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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

In the Matter of
CHICAGO RAILWAYS COMPANY and
CHICAGO CITY RAILWAY COMPANY,
Debtors.

CHARLES H. WORCESTER, RICHARD WAGNER and CYRUS MEAD, As a Committee for holders of Bonds of Chicago Railways Company, known as Series "B" Consolidated Mortgage 5% Bonds;

NAHUM BIRNBAUM and M. J. LUTTERMAN, Co-partners trading as Birnbaum & Company

JAMES A. COLE and CENTRAL HANOVER BANK AND TRUST COMPANY, Trustees, etc.

Petitioners,

vs.

CHICAGO TRANSIT AUTHORITY, et al.
Respondents.

Petition for a Writ of Certiorari to the United States Circuit Court of Appeals, Seventh Circuit.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

In the Matter of CHICAGO RAILWAYS COMPANY and CHICAGO CITY RAILWAY COMPANY, Debtors. CHARLES H. WORCESTER, RICHARD WAGNER and CYRUS MEAD, As a Committee for holders of Bonds of Chicago Railways Company, known as Series "B" Consolidated Mortgage 5% Bonds; NAHUM BIRNBAUM and M. J. LUTTERMAN, Co-partners trading as Birnbaum & Company JAMES A. COLE and CENTRAL HANOVER BANK AND TRUST COMPANY, Trustees, etc. Petitioners, vs. CHICAGO TRANSIT AUTHORITY. et al. Respondents.	Petition for a Writ of of Certiorari to the United States Circuit Court of Appeals, Seventh Circuit.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable The Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioners, Charles H. Worcester, Richard Wagner and Cyrus Mead, as a Committee for holders of Bonds of Chicago Railways Company, known as Series "B" Consolidated Mortgage 5 per cent bonds, Nahum Birnbaum and M. J. Lutterman, co-partners trading as Birnbaum & Com-

pany, James A. Cole and Central Hanover Bank and Trust Company, Trustees, etc., who represent and hold respectively numerous bonds of Chicago Railways Company, a Debtor herein, known as Consolidated Mortgage Series B, 5 percent of Chicago Railways Company, ([1]) respectfully pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit, affirming orders of the District Court of the United States for the Northern District of Illinois, Eastern Division, which had approved and confirmed a plan of reorganization for the debtor companies, as filed by Chicago Transit Authority, for acquisition of properties of debtors.

Chicago Surface Lines is an operating designation applied to the physical properties and operation in surface transportation in the City of Chicago of five companies. Chicago Railways Company and Chicago City Railway Company are the principal constituents. Two of the five companies are relatively small. A third, while larger than the two small companies are, represents a small percentage of the total properties. The companies are distinct as to corporate entity, indebtedness, outstanding securities and accounts, but all are integrated (since 1913) as to management and operation. The companies are identified in the

---

[1] The Petitioners' Charles H. Worcester, Richard Wagner, and Cyrus Mead III, acting as a committee for bonds of Chicago Railways Company known as Series B Consolidated Mortgage bonds, hold approximately $14,537,000 in principal amount of such bonds; Nahum Birnbaum and M. J. Lutterman, co-partners comprising a partnership under the name and style of Birnbaum & Co., Birnbaum and Co., a co-partnership consisting of Nahum Birnbaum and M. J. Lutterman, hold $225,000 in principal amount of said Series B bonds; Central Hanover Bank and Trust Company, a New York corporation, as Trustee, holds $33,000 in principal amount of said bonds; and James A. Cole holds $46,000 in principal amount of such bonds and also 319 Series 1, 200 Series 2, and 200 Series 3 participating certificates for stock of Chicago Railways Company.

initial paragraph of the opinion of the Circuit Court of Appeals.

It is noted here, however, that all the securities owned or represented by the petitioners are those issued by Chicago Railways Company. That Company in turn is the major constituent of Chicago Surface Lines, owning substantially 60 per cent of the properties embraced in the collective designation. The business and properties of the entity will be referred to as Chicago Surface Lines and it will be understood that the interest of Chicago Railways Company comprises generally 60 per cent of the aggregate so mentioned from time to time. The indebtedness of the respective companies does not, however, break in the same ratio as property values, earnings and expenses.

Nature of Proceedings.

The proceeding is one under Chapter X of the Bankruptcy Act, and the plan approved and confirmed by orders entered below contemplates a sale of the entire surface lines utility properties and a distribution of the proceeds in accordance with its terms.

Summary Statement of the Matter Involved.

Discontinuing consolidated equity receivership proceedings, the District Court on September 18, 1944, by orders entered in several causes consolidated for hearing, approved reorganization petitions filed under Chapter X, which had in turn been pending for some time, and appointed Trustees for each of three principal debtors. On February 28, 1945, City of Chicago filed a proposal and plan to acquire the Surface Lines properties, conditioning its offer upon simultaneous acquisition of the properties of Chicago Rapid Transit Company, a utility operating electric elevated lines, mainly in the City of Chicago, but extending also into some suburban areas. This proposal was

tentatively approved on preliminary hearing and referred to the Illinois Commerce Commission and to Securities and Exchange Commission. The latter filed its advisory report dealing with the two utilities on August 13, 1945. The report is not yet officially published in volume form, but will be found in full in CCH Bankruptcy Law Service, current opinions page 57683. It is identified as SEC release No. 65 of August 13, 1945.

Chicago Transit Authority was formed by legislative enactment of Illinois dated April 12, 1945. It is a municipal corporation, body politic, etc., and the validity of the creating Act was upheld by the Supreme Court of Illinois on November 21, 1945. *People etc.* v. *Chicago Transit Authority*, 392 Ill. 77. On August 17, 1945, Chicago Transit Authority, purporting to act as an assignee of the City of Chicago as to its right under the proposal and plan which City had filed on February 28, 1945 (which SEC disapproved) filed its own proposal and plan for the acquisition of the properties of Chicago Surface Lines. This document, later called a reorganization plan, was the plan approved February 27, 1946, by the first order appealed from below. At the conclusion of the hearings on the Plan the District Court referred the Chicago Transit Authority plan to the Securities and Exchange Commission for an advisory report. Such a report was filed on February 8, 1945 (Release No. 66). The document, not yet officially reported in SEC official volumes, apears in CCH Bankruptcy Law Service, current opinions, page 58026.

The Plan and proposal of Chicago Transit Authority was not submitted for consideration by the Illinois Commerce Commission.

While the appeal was pending from the order of February 27, 1946, aproving the plan, the plan was submitted

to security holders entitled by its terms to participate and upon affirmative vote it was confirmed by the District Court in order entered July 17, 1946.

The appeals from the two orders by the various parties were consolidated by order entered in the Circuit Court of Appeals on a single record and set of briefs and argument, were disposed of by that Court by one opinion filed January 4, 1947, and orders were entered affirming the orders appealed from.

Description of Properties.

Chicago Surface Lines system renders streetcar, gasoline and trolley bus services throughout the City of Chicago. Its trackage was increased from 586.34 miles in 1907 to 1,096 miles as of January 31, 1946. It owns 3427 street cars, 162 trolley buses, and 314 motor buses as of January 31, 1945 and now has on order (some of which have been delivered) 600 street cars and 675 buses. It carried over 891,000,000 revenue passengers in the year ended January 31, 1946 (fiscal year end). That carriage represents approximately 77 per cent of the local transit riders in Chicago, and the percentage has remained almost constant for many years. The gross revenues of the System for the year ended January 31, 1946, was $66,869,704.63.

The system represents an investment, computed in accordance with the 1907 Traction Ordinances hereinafter referred to, and not challenged, of $172,133,759.10 as of January 31, 1946.

Proceedings Below.

Chicago Transit Authority is not a creditor or stockholder of any debtor, and does not claim to be. It is a newly created entity, without substantial assets, without taxing

authority, or power to create liens upon properties it may acquire. In April 1945 it received from the City a franchise license to operate mass transportation facilities upon the streets of Chicago.

The order of the District Court in admitting the filing of its Plan by Chicago Transit Authority provided that it was entered without prejudice to the objection that said corporation was not in position to file a reorganization Plan in the proceeding, and the objections filed by the creditors on October 10, 1945, these petitioners included, specifically objected on this ground, viz:

> "It is axiomatic in this country that private property may not be taken for public use without just compensation. The legal methods of acquisition are condemnation or agreement.
>
> "Under Chapter X the parties to the proceedings are debtor, its creditors and stockholders (In re South State Ct. Bldg. Corp. 140 F 2d, 362 (at p. 366). Neither the City nor the Transit Authority comes within the definition of a party. The Act provides a manner and by whom plans may be presented. A prospective purchaser does not come within the definition of persons by whom plans may be presented.

It may be noted here that certain Committees of Bondholders, later entitled to participate under the Plan, filed a document in which they said that the Plan was joined in, etc., by the Committees representing all classes of creditors. Specifically the following words were used: viz:

> "This Plan is approved, adopted, joined in, and recomended to their respective depositors by the following Committees which represent every class of securities entitled to participate in this Plan."

In its opinion the Circuit Court of Appeals stated:

> "While it is true that it is the primary responsibility of the Trustee to file a plan of reorganization, here

> the trustees did file a plan and before its approval, the creditors of the debtor companies, in the form of a substitute plan, filed the present plan. Moreover, no objection was made by appellants to the filing of the plan by the City and the plan was adopted by other creditors who recommended its approval."

In essence and in fact this was not the situation presented. Moreover, no *creditor* filed the plan of Chicago Transit Authority, nor joined as such in the Plan. Certainly no creditor filed a plan, and even assuming a creditor or group of creditors, might file a plan for liquidation of debtor, no creditor sponsored this one. There is no representation or showing that the deposit agreements under which the signatory Commitees were formed in 1926 and 1927, ten years before Chapter X was enacted, authorized any of the Committees to take the action which the Circuit Court of Appeals impliedly attributes to them.

The Plan of Chicago Transit Authority proposes to acquire the utility properties of the Surface Lines, extensive non-utility properties (mostly vacant real estate) and certain reserve funds, for the sum of $75,000,000. The Companies are entitled to retain certain free cash, including an impounded item set aside annually after 1938 for payment of City compensation for street use, if adjudged to be due. The Plan provides that the properties be offered for sale at a fair upset price, and it states that the purchase is conditioned upon various matters, including the ability of the Authority to market its securities in a sum sufficient to raise the purchase price. Unless the securities may be sold advantageously, the offer is to be of no binding effect.

Included in the property to be purchased ("plan properties"), is a sum of approximately $25,000,000 in cash and also many materials and supplies on hand. The cash

owned by the respective companies (substantially 60 per cent by Chicago Railways Company or its Trustee), had been established under the provisions of the 1907 Ordinances, hereinafter mentioned, for the replacement or equipment depreciated or depleted in use. The net fund had accumulated over a period of time and was accordingly unproductive. The cash outlay to acquire these properties was accordingly about $50,000,000.

On the basis of the offer, first Mortgage Bonds of Chicago Railways Company, in principal amount of $41,741,250 will be discharged in full. Some $12,000,000 will be paid on Consolidated Mortgage Series A and Purchase Money Mortgage Bonds of the same Company, leaving a large deficit, and Consolidated Mortgage Series B Bonds, outstanding in the amount of $16,934,405 principal amount are entirely eliminated from participation, as is also a smaller issue junior to Series B.

From the foregoing it is apparent that the Plan before the Court was a liquidation and not a reorganization. The medium of sale at a fair upset price is in terms provided, but the District Court, accepting realities stated:

> Mr. Schroeder: Of course you have this to consider, that we are the bidder under this plan, and we have not bought yet, and maybe we won't be the highest bidder.
>
> The Court: Oh, now we are getting down to a point where this thing begins to look ridiculous.
>
> Mr. Schroeder: If you are sure of that, then that is all right.
>
> The Court: You are just as sure of that as you are that you are standing there. There is no possibility for any other bidder to appear under this situation here." (from Transcript of Proceedings June 10, 1946, p. 108).

Sharp differences arose on the hearing as to the method by which the property should be valued. These petitioners

took the position that as the proceeding was in effect an attempt by a public body to acquire a privately-owned utility property for public use, the proceedings should have been by condemnation, or if not, that the values should be fixed on the basis applicable under the condemnation law, or laws, which provide for public acquisition under "terminable permit" statutes which (though absent in Illinois) usually provide for the ascertainment and payment of a "fair value," "reasonable value," and the like. This method it was believed would give due consideration to the item of prudent investment and the cost of reproduction new, less depreciation. The latter figure as to Surface Lines properties, as the record shows, was $178,662,231. (PT 1038). Much evidence was taken as to the earnings, past, present and prospective; objector's evidence as to the prospective earnings took into account the probable yield after the expenditure of available cash for new, modern and economical equipment.

In the course of trial, counsel for Chicago Transit Authority, who took the burden of presenting evidence on the fairness of the plan, stated:

> "Mr. Schroeder: May I interrupt? (during testimony of Witness Fletcher.)
>
> "I object to this line of testimony as being immaterial, reorganization value in the sense of the issuance of new securities, as not being material to this inquiry because this plan does not contemplate the issuance of any new securities.
>
> "This might have been relevant in the prior hearing when new securities were to be issued, but not here." P.T. 1464).

While the findings of the District Court are very general, and find no statistical data, and furnish no estimate as to productivity in a future normal year, under varying conditions, we believe the Court, although it did not so

specify, stressed the earnings record and the prospects on a special theory which the Court developed, (and which will be later referred to as unfavorable to the security holders) to fix a market value, or fair upset price for the properties on sale and liquidation. It is believed that in the adjudicated cases the estimated earnings, capitalized, have been treated as sufficient only to govern the total capitalization and the allotment of securities of the reorganized companies; that is the situation which has usually been presented.

The findings by the District Court entered on February 27, 1946, are entirely silent on matters of earnings, past, present or prospective. A great deal of historical data relating to the proceedings in court, and the negotiations which led up to the filing of the proposals of the City and as to the later proposal by Chicago Transit Authority is stated, but as a substitute for stating or finding the elements of value of the properties the Court merely found:

> "Proposed Upset Price for Plan Properties is Fair.
> "The Court, in the exercise of informed and independent judgment under all the circumstances and upon all the data and upon specific consideration of prospective earnings of the properties of Chicago Surface Lines, finds that the sum of $75,000,000 upon the terms and conditions specified in Article II of the Plan is a fair, equitable and reasonable upset price for the Plan Properties. * * * * "

To this extent only did the court record by findings the basis upon which the fairness of the price was arrived at. The Court did not find or record any element of value; did not purport to estimate earnings of a future prospective year, nor determine what rate of capitalization should be applied. *Consolidated Rock Products Co.* v. *Du Bois*, 312, U. S. 510 certainly requires more specific and detailed findings. The exception or different rule applying in the cases

involving railroad reorganizations under Chapter 77, is based upon the fact that the duty of collecting and recording and appraising the facts there rests in the first instance upon the Interstate Commerce Commission, which acts substantially in a legislative capacity. There is nothing akin to a Commerce Commission report in the Chapter X proceeding, and the full duty of the court, to make concrete findings, exists as defined in the case cited.

In its opinion the Circuit Court of Appeals said:

> "It is clear that the court considered every proper factor suggested by the parties, and having in mind that an estimate as distinguished from mathematical certitude, was all that could be made, *Group of Investors* v. *Chicago, M. St. P. & P. R. R.*, supra, 542, it bottomed its findings of value upon all the evidence before the court * * *"

Estimates may be acceptable, as a practical matter, where new securities are being issued by a reorganized company, and alloted and apportioned to holders of original paper. Estimates should not be accepted in a case such as this.

The appeal, if allowed, will present the question as to the proper method of determining values where a liquidation of a vast utility, and the passing of private properties to public ownership is the end purpose of the proceeding.

Ordinances of 1907

The objections filed by the Petitioners below, deal at length with the rights and obligations under the 1907 ordinances which were worked out in reorganization of the much smaller properties owned to that date and passed on consummation to the three principal debtors in this proceeding. Under those reorganizations and pursuant to the 1907 ordinances the securities presently existing were

issued. The 1907 ordinances are of importance on several phases of this cause. It is not disputed that the ordinances evidenced or constituted a contract as between the City and the debtor companies. It is not denied that if claims made on behalf of the companies and on behalf of the security holders were sustained the fact would have far-reaching effect upon the values of the rights and properties. The Plan provides:

"G. Release of Claims.

"It is a condition of this Plan that the Trustees and Receivers, as the case may be, shall without any payment to them, waive, release and discharge (1) all claims to any right or interest in the tunnels and appurtenances under the Chicago River at N. LaSalle Street, just north of W. Van Buren Street, and at W. Washington Street, and to all public ways and public structures, and (2) all claims against the City of Chicago for loss or damage sustained from any cause whatsoever, including but not limited to loss or damage sustained by reason of the construction of the initial system of City-owned subways, and the Trustees and Receivers shall release and discharge the City from any and all such claims including but not limited to those based upon any ordinance, contract or agreement.

"It is also a condition of this Plan that the City of Chicago and the Authority, as the case may be, shall without any payment to either of them waive, release and discharge (1) any and all claims to or any right or interest in the escrowed Compensation Fund existing under orders of Court in the equity receivership and foreclosure proceedings, causes Nos. 6839 and 9915, and (2) all other claims of every kind, nature and description against the Companies or the Trustees or Receivers, including but not limited to those based upon any ordinance, contract, or agreement. The Authority has recommended to the corporate author-

ities of the City of Chicago that they waive and release all such claims upon conditions and terms herein provided in this Plan, and the City of Chicago has consented to such waiver and release."

If as the Circuit Court of Appeals states the rights under the settlement ordinances passed to the Trustees of Debtors, there is all the more reason that such rights should be valued and determined and that one standing in the position of Transit Authority, upon payment of the value of the physical properties (with cash reserves), at the price named in the Plan, should also pay something for the benefits which the City, not a party to the Plan receives or is to receive for the release which the trustees will in effect execute, and which will be released in effect by the bondholders also.

It has been the contention of these Petitioners that the Court should have determined the binding effect of the ordinance purchase price upon the City, and also upon the Chicago Transit Authority as the City's licensee to purchase. In the first place the lack of an operating ordinance or the right to obtain a new ordinance by a reorganized company, was mentioned by the District Court in its opinion of February 20, 1946, in discussing the hazards inherent in continued private ownership, difficulty of obtaining a bid by a private owner, etc. This reasoning followed largely the observations by the Security Exchange Commission in its report of February 8, 1946, wherein it was stated:

"The Objectors to the plan have taken the position that Surface Lines has the right to operate on the streets of Chicago until it is granted a new franchise or its properties are purchased at the price provided under the 1907 ordinance, amounting at this time to approximately $172,000,000. This contention is strongly opposed by the City and the Transit Authority. The Objectors' contention is primarily upon Section 23 of

the 1907 ordinance. The rights of the companies under this section, however, have never been judicially determined. In the absence of such judicial construction, the rights of Surface Lines to operate upon the streets are so beset with uncertainty that a separate valuation of Surface Lines would necessarily involve the use of a commensurately high rate of capitalization. It is our opinion, therefore, that separate valuation of Surface Lines based upon the capitalization of reasonably prospective earnings of the modernized property would require the use of a rate of capitalization so high, because of the unusual risk involved, that it would not exceed the valuation for Surface Lines as stated in our advisory report."

In another aspect a very substantial claim was presentable against the City if in its dealings with Chicago Transit Authority it breached the contract which it made in 1907 with the Companies, and with, or for the benefit of, the security holders.

Determination of the residuary rights under the 1907 ordinances was important from the standpoint of basis for city compensation for use of streets, the right to remain upon the streets, the removal of obstacles as to future use by a private owner, and the position of a private owner to negotiate with the city.

A third point which the court did not decide was whether the rights of the various classes of securities of Chicago Railways Company, arising from the covenants in the Consolidated Mortgage that the obligations of the City under the purchase provisions of the ordinances, should be protected and preserved for the security holders.

These points, suggested here, will be developed in the brief filed herewith.

Petitioners also contended below and will seek to contend here in this Court that liquidation of these properties was untimely, the Trustees of Debtor not having reported that a reorganization was not feasible.

Principal Contentions

Petitioners' contentions emerge from the fact that the District Court and the Circuit Court of Appeals:

Completely wiped out the claims of the Series B Bondholders against the City of Chicago under a certain traction ordinance of 1907 under which the City agreed either to purchase the traction lines affected by the Series B Mortgage or to require any other company to whom the City would grant a franchise to operate these lines to purchase the same at a price computed under a stated formula. Admittedly the City took neither action. Section G of the Plan expressly releases the City of Chicago from such claims despite the fact that the City is not a debtor herein—thus destroying the rights of the B Bondholders without compensation and without due process of law. In the light of the express release of these rights against the City, the Circuit Court of Appeals was clearly in error in sustaining the plan on this score upon the ground that the claim against the City became part of the estate enforceably by the Trustee for the benefit of the B bondholders and other creditors.

Disregarded certain contractual engagements among the Series B bondholders, senior security holders and the City of Chicago, which, in Petitioners' view, should have precluded and estopped the senior security holders from assenting to the present plan and thereby the District Court undertook to rescind or dissolve contractual obligations subsisting independently of the debtor companies, not

forming either assets or liabilities of such companies, and therefore not subject to the *in rem* jurisdiction of the Court.

Instead of sustaining Petitioners' contention that the Companies had a contractual right under the ordinances of 1907 to occupy Chicago streets until paid an "ordinance purchase price" provided by such ordinances, expressed judicial "doubts" as to such rights without resolving such "doubts" permitted such alleged "doubts" to debase the value of the property upon the theory that they constituted a cloud upon the companies' title. The Court then made the value of the property as depressed by such "doubts", the basis for finding a valuation so low as to disentitle petitioners to participation under the Plan.

Found that the companies were entitled to a ten-cent instead of an eight-cent basic fare, authorized its Trustees to apply to Illinois Commerce Commission for such fare, adopted "capitalization of projected earnings" as a basic criterion of valuation, but refused either to await the outcome of the application to the Commission or to assume that such application would be granted, refused to project earnings upon the basis of a prospective basic fare greater than eight cents, and then upon prospective earnings thus projected on the lower fare found valuation so low as to preclude "B Bondholders" from participation under the plan.

Refused in its memorandum opinion of February 20, 1946 to give effect to probable earnings after modernization of the Lines in adopting $4,000,000 as earnings for the purpose of determining capitalized value of the utility properties.

Otherwise so far departed from the judicial concepts of value and Congress' and this Court's norms of intrastate public utility valuation (a) for reorganization purposes, and (b) for acquisition by governmental purchase for pub-

lic use, as in the instant case, that the court's pronouncement of "value" fails as a matter of law to respond to such concepts and norms, wherefore petitioners say the court's pronouncement of "value" is not a judicial finding of "value" within the purview of Chapter X of the Bankruptcy Act.

Approved the plan although its own trustees had not been directed to formulate and had not in fact formulated any plan for the reorganization or rehabilitation of the debtor companies or any of them, or reported their reasons why a plan could not be effected.

Fixed as a sale price, in a proceeding to pass these properties to public use and ownership, the value in substance measured by the "estimate" as distinguished from "mathematical certitude" held suitable in the fixing of permissible capitalization and allocation of securities in continuing a business on a reorganized basis.

Permitted Chicago Transit Authority, not a creditor or a stockholder of any debtor in this proceeding, to file and prosecute under the appellation of a reorganization plan, a proceeding to acquire these private properties.

Approved the plan without first submitting it to the Illinois Commerce Commission, although the debtor companies operated a wholly intrastate public utility subject to that Commission's jurisdiction and although submission to such Commission is a statutory jurisdictional prerequisite to approval.

Made insufficient determination and findings of questions of fact, relating to the business, property and rights of debtors.

The Questions Presented.

Whether the Courts below erred—

1. In failing to determine questions presented under the ordinance of 1907, as to the liability of the City of Chicago and of Chicago Transit Authority, as the holder of an operating franchise from the City, to pay the ordinance purchase price on the acquisition of the utility properties of the debtors, and as to the residual rights to operate on the public streets until the ordinance purchase price should be paid or until a new franchise should be granted to debtors?

2. In approving a plan which embodied, without consideration, a release to the City of Chicago of all claims based upon any ordinance, contract or agreement? And in approving a plan which granted similar releases, also without consideration, to Chicago Transit Authority?

3. In extinguishing so large an amount of secured indebtedness of debtor (A) without taking into account earnings projected on the basis of an increased fare and results of modernization, (B) by depressing the value of the property on account of doubts as to the Debtors' rights in the City streets, until paid the ordinance purchase price, which doubts the Courts should have resolved, and (C) by otherwise so far departing from juridical concepts of valuation as to confiscate petitioners' property rights?

4. In abrogating or annulling contractual rights among the Series B Bondholders and the senior issues, *inter sese* and with the City and the Transit Authority, which rights were neither assets nor liabilities of the debtor, but belonged to security holders?

5. In approving the plan of Chicago Transit Authority

without first submitting it to the Illinois Commerce Commission?

6. In approving the plan when its trustees had not previously filed a plan for the reorganization of debtor companies, apart from a merger with the elevated lines of Chicago Rapid Transit under an ordinance (tendered) which required merger and common ownership of the two systems, and in approving a plan for the liquidation of debtor companies in advance of such a recommendation by the Trustees or a report by them of reasons why a reorganization could not be effected? And in permitting a prospective purchaser, not a creditor or stockholder of the debtor to file and prosecute a plan for liquidation?

7. In the manner of fixing the upset price at which the properties might be acquired by a public body, and in failing to require the payment of an adequate and reasonable price on such acquisition?

Reasons Relied on for the Allowance of the Writ.

1. In order that proper procedure may be outlined and directed and erors corrected:

A. As to the method of determining the value of the plan properties in a case of this character where the properties are gigantic and liquidation is the sole objective of the Plan.

B. In order that an authoritative ruling may be had as to the stage at which a reorganization proceeding may be converted into a procedure for liquidation, and as to the methods prescribed by Chapter X to accomplish such a result.

C. In order that proper limitations may be placed upon the rights of non-creditors seeking to purchase the properties to proceed as parties in a Chapter X case.

D. In order that the properties here involved may be valued for purposes of sale in such a manner as to reflect the proper value for acquisition by a public body, seeking to acquire private property for public use and in view of the contracts embodied in the 1907 Franchise Ordinances.

E. In order that the rights of the Debtors and the security holders against the City of Chicago, under the 1907 Ordinances and the basic agreements, may be determined and valued for sale or reorganization, or preserved until equitable disposition, based on consideration moving from the City to the Trustees or the security holders, may be accomplished.

F. In order that proper findings may be required of the District Court for valuation or the fixing of an upset price if sale be ordered.

G. In order that a determination may be had of the propriety of approving and confirming the plan of Chicago Transit Authority without its prior submission to the Illinois Commerce Commission, pursuant to Sec. 178 of Chapter X and without prior compliance with the mandate of Sec. 169 of Chapter X.

Opinions Below.

At this date neither the opinion of the District Court on approval of the plan, nor the opinion of the Circuit Court of Appeals affirming the approving and confirming orders has been officially published. Leave to supply the citations, when available is asked.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on January 4, 1947. The jurisdiction of this Court in invoked under Section 240 of the United States Judicial Code. (28 U.S.C.A., Sec. 347). It is believed the granting of the petition is justified for that the case presents important problems under Chapter X of the Bankruptcy Act, having relation to the effective administration of corporate reorganizations. Petitioners also contend that the judgment appealed from deprived the security holders represented of their property, without due process of law, in violation of the Fifth Amendment.

Statutes Involved.

The issues involve the construction and application to the facts of this case of Chapter X of the Bankruptcy Act (11 U.S.C.A. §501 etc.).

WHEREFORE, your petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Seventh Circuit, commanding that court to certify and send to this Court for its review and determination on a day certain to be therein named, a full and complete transcript of the record and all of the proceedings in the cases numbered on its docket, Nos. 9057, 9136, 9189, 9059, 9137, 9190, 9122, 9191, 9192 and 9193, all consolidated and heard as a single case in that court and entitled, In the Matter of Chicago Railways Company, Debtor, Chicago City Railway Company and Calumet and South Chicago Railway Company, Debtors, and that the judgment of the Circuit Court of Appeals for the Seventh Circuit may be reversed and the orders of the District Court may be

reversed, and that your petitioners may have such other and further relief in the premises as to this Court may seem proper.

CLYDE E. SHOREY,
JOHN E. GAVIN,
WILLIAM RUFUS MORGAN,

Attorneys for Charles H. Worcester et al., as a Committee, etc., Nahum Birnbaum et al, doing business as Birnbaum & Company, and James A. Cole and Central Hanover Bank and Trust Company, as Trustee, etc.,

Petitioners.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

A Subject Index of the matter in the brief, with page references, and a Table of Authorities will be found immediately preceding the Petition.

SUMMARY OF ARGUMENT.

I.

The lower courts, instead of deciding that the 1907 Traction Ordinances gave the companies the right to occupy the streets of Chicago until the companies should be paid the ordinance purchase price, expressed judicial doubts on the question. The lower courts then permitted these "doubts" to depress the "fair market value" of the properties. The lower courts used the value of the properties as thus depressed by these unresolved doubts as the basis for holding that petitioners had no interest in the properties; and in effect the lower courts refused to decide what property rights were to be exposed for sale.

The lower courts undertook to release the City and the Transit Authority from the contractural obligations imposed by the ordinance without determining what those rights were.

Thus the lower courts, by refusing to adjudicate the rights of petitioners, deprived them of their property without due process of law; for to abrogate contractural rights without ascertaining what they are is to deny the essential substance of a hearing.

The Ordinance Price of approximately $172,000,000, which, with free cash, would have been more than sufficient

to pay the B bondholders in full, should have been the minimum figure at which the properties could be sold to the Transit Authority, as privy of the City.

II.

The indentures securing the senior securities and the Series B bonds, when integrated with the contractural provisions of the 1907 Traction Ordinance, constituted a contract among the senior security holders, the Series B bondholders, and the City. This contract was neither an asset nor a liability of the debtor. Therefore the District Court had no right to undertake to abrogate or release the contract rights of the Series B bondholders against the senior security holders and the City.

III.

The District Court found that the companies were entitled to a ten-cent basic fare, authorized its trustees to make application to the Illinois Commerce Commission for an increase from the present eight-cent fare to ten cents, adopted "capitalization of earnings" as the basic criterion of value, and then, instead of either assuming that the Illinois Commission would grant the increase or awaiting the event of the application therefor, projected earnings on the basis of an eight-cent fare.

In the Argument it is shown that if earnings are projected on the basis of a ten-cent fare, without other corrections of the lower courts' methods of valuation, the Series B bondholders would be entitled to participate in any fair plan of reorganization.

IV.

The District Court's Valuation of the Debtor's Properties, upon which valuation the propriety of excluding Series B bondholders from the plan depends, does not respond to juridical concepts of value.

A.

The District Court treated the Transit Authority's offer as evidence of the maximum value of the property, thereby allowing such offer to justify itself.

B.

The Securities and Exchange Commission's valuation, when reconstructed to allow for (a) a ten-cent fare, (b) resolution of doubts as to the companies' rights in the streets, (c) reorganization of the Surface Lines without the Elevated Lines, and (d) effects of a modernization program, supports a valuation admitting Series B bondholders to participate in distribution.

C.

A prior finding of approximately $136,000,000 as a "valuation of the properties for reorganization purposes" affords a minimum basic figure in this case, to which figure must be added other assets some of which were not valued by the Court.

D.

This court should not itself determine the valuation of the properties. It should remand the cause for redetermination by the District Court in accordance with proper principles.

V.

The orders appealed from were not only erroneous but void because the trustees were not directed either to "file a plan or a report of reasons why a plan cannot be effected." Section 169 makes such a direction to trustees and compliance therewith prerequisite to the approval of any plan.

VI.

The orders appealed from were not only erroneous but void because the plan was never submitted to the Illinois Commerce Commission.

Reference to the Opinions of the Lower Courts.

Neither the District Court's opinion nor the Circuit Court's opinion has been reported. The District Court's opinion, which was dated February 15, 1946, and spread of record February 20, 1946, will be found at p. 3472 of the transcript. The order approving the plan, which was entered February 27, 1946, will be found at p. 3473 of the transcript. The order confirming the plan, entered June 17, 1946, will be found at p. 4461 of the transcript. The decision of the Circuit Court of Appeals, dated January 4, 1947, will be found in full in the transcript of the Circuit Court of Appeals record.

Statement of the Grounds on Which the Jurisdiction of the Court is Invoked.

This court's jurisdiction is invoked under Section 240 of the United States Judicial Code (Title 28, U.S.C.A., Section 347). The decision below was pronounced January 4, 1947, and within three months prior to the filing of this petition.

STATEMENT OF THE CASE.

The Petition, *ante,* sets forth the general nature and extent of the properties and the enterprise which are the subject matter of this case. It also briefly states the substance of the plan for the sale of those properties. We omit repetition of such description in the interest of brevity.

In the present Statement, we present the substance of the factual data necessary to an understanding of the issues that we intend to argue.

The 1907 Traction Ordinances.

In 1907, reorganizations or consolidations of fifteen previously existing companies resulted in the existence of the five companies mentioned above.

At the time of these 1907 reorganizations and consolidations, the City of Chicago adopted two "Traction Ordinances" which, together with two further ordinances adopted in 1908 and 1909, created and defined contractual rights, very important in this case, among the City, the companies, and the companies' security holders. The Chicago Railways Company Ordinance is printed in material part at pp. 1 to 37 of Petitioners' Appendix.

Provisions for the purchase after 1927 at not less than the "ordinance purchase price": The ordinances embodied covenants whereby the City reserved the right to purchase the companies' properties prior to February 1, 1927, for a base price fixed in the ordinance plus the value of additions and extensions at a figure to be approved by the Board of Supervising Engineers, an agency created by the Ordinances and one member of the Board was designated by the

City. The Ordinances further provided that if the City or its licensee should not purchase the properties on or before February 1, 1927, and if the City should thereafter designate a licensee to purchase the property or grant a new franchise or ordinance to another company, then the City or such licensee or company should be obligated to pay for the properties a price computed under the terms of the ordinance. Section 23 of the ordinance is quoted in the margin.[2] The provisions of the Ordinances were authorized by the so-called "Mueller Law,"[3] which was adopted by the Illinois Legislature in 1903 as an enabling act passed in contemplation of a solution of Chicago's then existing traction problem.

It is not disputed that the ordinance purchase price, as of January 31, 1946, would have been $172,133,759.10; nor is it disputed that Chicago Railways Company's share of this value (approximately 60% thereof), plus the free cash of that company, would be sufficient to pay the Series B bonds in full after the complete discharge of all prior liens. The validity of the computation is not challenged. The procedure observed in establishing the ordinance purchase price appears in the record. (Pet. Appendix 129-130; 22 Ill. C. C., 682-83.)

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[2] "Rights of Company in Case City Does Not Purchase For Twenty Years.

"Section 23. In the event that the said street railways are not purchased by the said City or its licensee as hereinabove authorized, prior to February 1, A. D. 1927 (and nothing in this ordinance contained shall be construed as being in any event a grant to the Company extending beyond February 1, A. D. 1927), the said City shall have the right to designate any person, firm or corporation having lawful authority to acquire, own and operate street railways in said City as its licensee, to purchase the said street railways property and rights of the Company at or after February 1, A. D. 1927, upon the same terms that the City could then purchase, and in case such reserved right of purchase be not exercised by the said City or its licensee and the City shall grant a right to another company to operate a street railway in the street and parts of streets constituting the said street railway system of the Company, such new company shall be required to and shall purchase and take over the said street railways, property and rights of the Company at or after February 1, A. D. 1927, upon the same terms upon which the said City might then purchase and take over."

[3] Section 1 of the Mueller Law appears, in part, as Appendix I to the brief.

The 1907 Ordinances constituted one of the basic contracts upon the faith of which the 1907 reorganization was accomplished.[4]

The Securities and Liens Involved in This Case.

So far as Chicago Railways Company is concerned, the paramount claim is that of the first mortgage bondholders, who will be paid in full under the plan. The aggregate unpaid principal due upon the first mortgage bonds is $41,741,250.

Two junior issues of Chicago Railways Company bonds here involved, Series A and Series B, respectively, are secured by a "consolidated mortgage" dated as of February

[4] In the decree fixing amount and priority of liens entered July 18, 1928 by the District Court in Case No. 6839 (Chicago Railways Company), the court found:

"The Plan of Reorganization and Readjustment which is referred to in Section 1 of the Ordinance of February 11, 1907, and in the Agreement "Exhibit D" to said Ordinance, was duly promulgated by the Railways Company and approved as in said Ordinance and Agreement provided, and thereupon was declared and became effective for the release and discharge of all interests, rights, liens and claims against the properties of any of the Companies formerly owning or interested in any of said properties, and entitling them to receive the new securities provided in said Plan to be issued, and which were issued by Chicago Railways Company in exchange for those which the several holders of the old rights had thus released and surrendered. * * *

"Said Plan also provided for the execution of:

'A Consolidated (or second) Mortgage, to secure issue of 20-Year Gold Bonds, aggregating not to exceed Thirty-Seven Million Five Hundred Thousand Dollars ($37,500,000.00). Fifteen Million Nine Hundred Thousand Dollars ($15,900,000.00) of these bonds were to be of Series "A", having priority in all respects over bonds of Series "B" and "C"; and Sixteen Million Nine Hundred Thousand Dollars ($16,900,000.00) of said bonds were to be of Series "B", having priority in all respects over bonds of Series "C". Not exceeding Four Million Seven Hundred Thousand Dollars ($4,700,000.00) issued under said mortgage were to be of Series "C".'

"None of the bonds of Series 'C' are unpaid and outstanding.

"Said Plan by further provisions authorized the issue, and there were duly executed and issued under said Plan, and said Consolidated Mortgage, bonds of Series 'A' to the total amount of Eighteen Million Six Hundred Thousand Dollars ($18,600,000.00), and bonds of Series 'B' to the total amount of Seventeen Million One Hundred and Ninety-four Thousand Dollars ($17,194,000.00).

"The Consolidated Mortgage referred to in this decree is the mortgage thus provided for in said plan, and was executed in conformity therewith." (Pet. Appx. 87-89.)

1, 1907, which was of even date with the first mortgage but is subject in lien thereto (Tr. 176). Under the provisions of the consolidated mortgage, the lien of the Series A bonds is superior to that of the Series B bonds.

All rights of the Debtor, Chicago Railways Company, under the 1907 Ordinance were subjected to the lien and charge of the consolidated mortgage. (Pet. Appx. pp. 47-49.)

The Consolidated Mortgage contained a covenant to the effect that the liability of the City, its licensee or designated nominee, or new company, to pay the ordinance purchase price should never be "impaired, or suspended, or reduced, or abated, or subjected to the risk or danger of forfeiture, annulment, impairment, or suspension, or of a reduction or an abatement" until the Series A and Series B bonds should be paid in full, or until the ordinance purchase price should be paid in full. (Pet. Appx., subparagraph y, pp. 56 and 57.) [5]

[5] (y) Will not do, or suffer, cause or permit to be done or occur, any act, thing or event by reason or as a result of which (1) the possession by the Railways Company of any part of the street railways system mentioned in the Ordinance, or the right of the Railways Company to have, receive or retain all or any part of any of the sums mentioned as being payable to or as belonging to the Railways Company, in the event that, or so long as, each and every the terms, conditions, provisions and limitations in the Ordinance set forth, are kept performed, observed and complied with, and if and so long as no default shall occur in respect of any of them, will, or may become impaired, suspended, terminated, annulled, or forfeited, or be subjected to the claim or danger thereof; or (2) the liability or obligation of the city of Chicago or of any licensee or nominee of said city, in case of a purchase or a taking of possession by said city, or its licensee, or by a nominee designated or authorized by said city to make a purchase or take possession, of the street railway system mentioned in the Ordinance, or any part thereof, to pay in full, the several amounts or percentages mentioned or provided in sections twenty, twenty-one, twenty-two and twenty-three of the Ordinance, will or may become impaired, or suspended, or reduced, or abated, or subjected to the risk or danger of forfeiture, annulment, impairment or suspension, or of a reduction or an abatement; or (3) any of the rights, privileges, grants, or benefits in the Ordinance contained, or which may hereafter be granted to or acquired by the Railways Company for use in connection therewith, will or may be subjected to the risk or danger of forfeiture, annulment, suspension, interruption or impairment."

The Series A and Series B bonds and the Consolidated Mortgage were issued in accordance with the 1907 reorganization plan and upon the terms and conditions and in accordance with requirements provided in the 1907 ordinances. (Pet. Appx., pp. 38-43.) The contract provisions and rights under the ordinances constituted an inducement to the acceptance of the plan and the acceptance of the new securities, namely, the Series A and Series B bonds (Appx., pp. 38-43; footnote 4, *ante.*) Therefore, the ordinance rights, particularly under Section 23 thereof, constitute a contract between the Series A and Series B bondholders *inter sese* and a contract between the Series B bondholders and the City of Chicago.

The City of Chicago granted to Chicago Transit Authority an ordinance franchise dated as of April 23, 1945. Petitioners say that the granting of such ordinance created an immediate liability under Section 23 of the 1907 ordinance to pay the ordinance purchase price for the properties in question.

The title of the trustees to the property of Chicago Railways Company, Debtor, and their rights under the ordinance are in all respects subject to the lien and covenants contained in the Consolidated Mortgage. But the plan provides in Section F (Tr. 3231, p. 20-21) not only that the property of the *debtors* shall be conveyed free of the lien of the Consolidated Mortgage, but that all rights against the City, including the contractual rights of the Series B bondholders, **which subsist directly against the City and the Transit Authority, and which are neither assets nor liabilities of the Debtors,** shall be released directly to the City (Section G, Tr. 3231, p. 22). Thus by approving and confirming the plan, the lower courts sanctioned the release of the consolidated mortgage securing the Series B

bonds and the granting of release to the City, without any compensation, of all rights under the 1907 ordinance, thereby impairing the obligations of contracts and destroying the property rights of the Series B bondholders against the City and the Transit Authority without compensation and without due process of law.

Petitioners' Claims of Rights Founded on the Traction Ordinances and the Consolidated Mortgage.

Petitioners contended below and seek to contend here that the 1907 Traction Ordinances, as construed by the Supreme Court of Illinois in *Venner* v. *Chicago Railways Company*, 203 Ill. 349, and *Harris Trust and Savings Bank* v. *Chicago Railways Company*, 39 Fed. (2d) 958, those decisions being *res judicata* so that the question is no longer open, gave to the companies the right to occupy the city streets until the ordinance purchase price should be paid; and that the general mortgage constituted a contract among the Series A and Series B bondholders that the companies' properties would never be sold to the City or its licensee or "another company" for less than the ordinance purchase price unless the Series A and Series B bondholders were paid in full.*

Petitioners further contended that since this contract among the Series A and Series B bondholders *inter sese* was neither an asset nor a liability of the company, it could not be abrogated or dissolved by order of the District Court in this case because the Court lacked jurisdiction to rescind contractual engagements among parties who were not in bankruptcy and whose estates and obligations were not before the court.

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* This position was taken by the Trustees of the Debtor (Tr. 2663, p. 2).

The Petitioners say that to approve the plan with Sections F and G therein, which required the release to the City of all claims and rights under the 1907 ordinance, denied to the Series B bondholders rights guaranteed by the Fifth and Fourteenth Amendments to the Constitution of the United States.

The District Court Refused to Decide the Franchise Ordinance Questions and Thereby (A) Failed to Adjudicate the Contract Rights of Petitioners and (B) Failed to Define the Property Rights That It Exposed For Sale.

Petitioners contend in their brief, *post*, that the companies' right to occupy the city's streets until paid the ordinance purchase price was absolute and argue that the District Court should have sustained this contention. But the District Court, instead of sustaining this contention, said that a prospective purchaser might treat it as doubtful.

The District Court then said that such putative "doubts" on the part of a hypothetical prospective purchaser would, diminish the price that such a purchaser would be willing to pay for the property, wherefore the Court reasoned that the valuation of the companies' properties was depressed by the presence of these unresolved "doubts."

Then the District Court used the value of the property as thus depressed by such unresolved doubts as a basis for declaring that Petitioners had no interest in the companies' properties.

Petitioners contended below and seek to contend here that since the Court had jurisdiction of the City and the companies, it should have decided the important question, so raised by it, of the companies' rights in the city's streets until paid the ordinance purchase price. Petitioners further contended below and seek to contend that it should

have decided these questions favorably to Petitioners. And Petitioners contend that the Court's treating these questions as unresolved doubts instead of deciding them not only unfairly depressed the *value* of the properties offered for sale, but actually amounted to refusal to define or determine *what property it proposed to offer for sale under the plan,* which contemplates (although it renders practically impossible) purchase by a possible competitive bidder at the sale.

This refusal to decide these questions also amounted to a refusal to define the rights that the District Court released to the City.

The District Court's Projection of Earnings on the Basis of an Eight-Cent Fare, Notwithstanding Its Finding That the Companies Were Entitled to and Might Anticipate a Ten-Cent Fare.

The District Court purported to adopt "prospective earnings" as its basic criterion for valuation. It found that the companies were entitled to a ten-cent basic fare (with appropriate adjustments for children's fares, inter-company transfer fares, etc.). It authorized its trustees to make application for such ten-cent basic fare to the Illinois Commerce Commission. Such application was made and is now pending.

But the Court refused either to assume that the application would be granted or to await the actual outcome of the application. Instead, it projected earnings upon the hypothesis of a continuation of the present eight-cent basic fare. In this brief, *post,* Petitioners demonstrate that if earnings were projected upon a ten-cent fare, the properties would sustain a valuation on earning properly capitalized which would entitle Series B bondholders to participate in distribution under any plan.

Other District Court Rulings with Respect to Valuation of Which Petitioners Seek to Complain.

In the brief, we undertake a demonstration that the District Court did not give effect to the increased patronage and to the economy certain to result from a full modernization of the system, for which modernization the record disclosed that the companies have cash on hand in the aggregate sum of approximately $4,000,000.[7]

The District Court professed to find support for its valuation in a report of the Securities and Exchange Commission. But that Commission's advisory report was based upon a valuation of the properties depressed by alleged doubts as to title, which doubts that Commission could not resolve and the District Court could have resolved. Moreover, the actual report contemplated not a sale of the Surface Lines properties alone but a consolidation or other amalgamation of those properties with the properties of the Rapid Transit System. This valuation of a hypothetical amalgamated system took into account the fact that the Rapid Transit Company is sustaining a constant loss, so that its integration with the Surface Lines properties would, from the point of view of prospective earnings (although of course not from the point of view of invested capital), depress rather than enhance the valuation of the hypothetical amalgamated system as an entirety. Petitioners undertake a demonstration that when the Securities and Exchange Commission's report is properly interpreted, it does not support the Court's valuation. (See Brief, *post.*)

As will be demonstrated in the brief, *post,* the Commission's valuation of the combined Surface Lines and the Rapid Transit property had the effect of depressing and confiscating the value of the Surface Lines property. The

[7] Renewal Funds and free cash assets. (See plan, Tr. 3231, p. 36).

record demonstrates (P. T. 1050-1081) that when the Surface Lines component element of the combined valuation as made by the SEC in its advisory report is segregated, and all elements and factors used and observed by the SEC in determining its combined value are followed, the value of the Surface Lines property alone would be $123,708,000. The Securities and Exchange Commission in its supplemental report stated (Tr. 3443, p. 14): "In our opinion, $7,000,000 is a liberal estimate of prospective earnings after modernization before Federal taxes and fixed charges for Surface Lines as a separate operation." Furthermore, *this projection was on the basis of an eight-cent fare,* instead of the ten-cent fare to which the Court found that the companies were entitled. And the SEC further stated (Suppl. Report, pages 15-16):

> "The Objectors to the plan have taken the position that Surface Lines has the right to operate on the streets of Chicago until it is granted a new franchise or its properties are purchased at the price provided under the 1907 ordinance, amounting at this time to approximately $172,000,000. This contention is strongly opposed by the City and the Transit Authority. The Objectors' contention is primarily upon Section 23 of the 1907 ordinance. The rights of the companies under this section, however, have never been judicially determined. In the absence of such judicial construction, the rights of Surface Lines to operate upon the streets are so beset with uncertainty that a separate valuation of Surface Lines would necessarily involve the use of a commensurately high rate of capitalization. It is our opinion, therefore, that separate valuation of Surface Lines based upon the capitalization of reasonably prospective earnings of the modernized property would require the use of a rate of capitalization so high, because of the unusual risk involved, that it would not exceed the valuation for Surface Lines as stated in our advisory report."

It is obvious that the Court's failure to adjudicate the ordinance question resulted in a depression of the value of the Surface Lines property. Not only is this true, but by releasing the rights under the ordinance to the City of Chicago without compensation, the Court undertook to release by approving and confirming the plan the rights and properties of the Series B bondholders without any compensation therefor.

The District Court failed to take account of the factors requisite in valuing public utility property under the Illinois law of public utility regulation and eminent domain. These factors, Petitioners say, were relevant not because the District Court, sitting in bankruptcy, is controlled by Illinois Law, but because it undertook the task of projecting earnings and determining property rights which would be largely controlled by Illinois law. Hence Illinois law woud be relevant to any prognostication of earnings to be fixed under that law.

Sundry other serious criticisms are made of the Court's valuation in the brief. It would be inappropriate to indicate the detailed basis for those criticisms here.

The Court's Trustees Were Not Directed to Formulate and Did Not Formulate Any Plan of Reorganization for the Debtor Companies Prior to the Approval of the Present Plan.

Although Section 169 of Chapter X requires that the court's trustee (or trustees) "shall prepare and file a plan, or a report of his reasons why a plan cannot be effected" and that the court shall "fix a subsequent time for a hearing on such plan or report," the Court's trustees were never directed to formulate and did not in fact formulate any

plan for the reorganization of the debtor companies. Nor did the Trustees file any report of their reasons why a plan could not be effected.[8]

The Trustees filed suggestions and objections to the City proposal and the Advisory Report of the Securities and Exchange Commission thereon, which point out basic errors in the instant proposal. (Tr. 3145.)

The District Court Failed to Submit the Plan to the Illinois Commerce Commission.

Notwithstanding the provisions of Section 178 of Chapter X of the Bankruptcy Act, which require that no plan for a wholly intrastate public utility debtor shall be approved unless the "State commission of the regulatory jurisdiction over such debtor" shall "have first certified its approval of such plan as to the public interest therein and the fairness thereof," the District Court did not submit the present plan to the Illinois Commerce Commission. That Commission has always possessed plenary regulatory authority over the debtor companies, as the District Court recognized when it directed its trustees to apply to that Commission for an increase in fares.

The Opinion of the Circuit Court of Appeals.

We do not undertake to summarize the opinion of the Circuit Court of Appeals, which of course appears in full in the transcript of the Circuit Court record. We do, however, quote and emphasize the following excerpt therefrom:

"True, Section 23 does provide that if, after the

[8] The Trustees did at one time in the history of these Chapter X proceedings undertake to formulate a plan, dated as of November 29, 1944, for the unification of the debtor companies with the Elevated Lines. But that plan was, of course, not one for the reorganization of the instant debtor within the purview of Chapter X. It was disapproved by the Illinois Commerce Commission by its order or report of June 5, 1945. (Tr. 3640.)

> expiration of the ordinance, the City should grant a franchise to a new company, the new company shall buy the property upon the terms upon which the City might have purchased. Even so, that fact, under the circumstances in this case, is no reason why the plan should not be approved, since all contingent rights of a debtor pass to its trustee and become part of its estate, *Pollack* v. *Meyer Bros. Drug Co.*, 233 F. 861, and may be dealt with in Chapter X proceedings."

Thus the Circuit Court of Appeals sanctioned the District Court's failure to adjudicate the rights of the debtors and the independent rights of their security holders, including Petitioners, to occupy the streets of the City of Chicago, until such time as the ordinance contract purchase price should be paid. Thus the Circuit Court of Appeals approved a valuation debased by a failure to define the rights that were being offered for sale.

Similarly, the Circuit Court of Appeals failed to recognize that the contract rights of the security holders are independent of those of the debtor, were neither assets nor liabilities of the debtor, subsisted among the security holders *inter sese,* and were not subject to disposition by the Court.

This petition asks this court to determine the important question whether a court of bankruptcy may, as a purported incident to a plan for the liquidation of a debtor, abrogate or alter the contract rights of various classes of security holders, respectively, *inter sese.* The Circuit Court of Appeals did not pass upon this question.

Petitioners assert that inasmuch as they have had no decision of these important questions, and have encountered with respect to the question of valuation a refusal to decide them, they have been denied due process

of law, and that their property is being expropriated for public use not only without a fair determination of just compensation but without any determination at all upon that question.

Specifications of Errors Intended to be Urged.

1. The lower courts erred (A) in refusing to hold that the companies had the right to occupy Chicago's streets until paid the ordinance purchase price in accordance with Section 23 of the 1907 Ordinance, (B) in refusing to hold that under the indenture securing the Series A and Series B bonds, this right could not be released without the consent of the Series B bondholders and (C) in refusing to determine that the Ordinance purchase price should be the minimum sale price for the properties.

2. The lower courts erred in depressing the valuation of the properties of the Debtors (A) by expressing, instead of resolving, judicial doubts as to the rights in the streets, (B) by projecting earnings on the basis of an eight-cent fare when it had found that they were entitled to a ten-cent fare, and (C) in otherwise so far departing from juridical *criteria* of value that its pronouncement does not respond to any concept of "valuation" enacted by the Bankruptcy Act.

3. The District Court erred in approving and confirming the plan when its trustees had not previously been directed to file and had not filed a plan for the separate reorganization of the Surface Lines in accordance with Section 169 of Chapter X of the Bankruptcy Act.

4. The District Court erred in approving and confirming the plan when it had not been submitted to the Illinois Commerce Commission in accordance with Section 177 and 178 of Chapter X.

ARGUMENT.

A Summary of Argument appears immediately after the Index and table of Authorities and immediately preceeding the Petition, *ante*.

I.

The Lower Courts Erred (A) in Refusing to Determine the Rights of the Companies Under Section 23 of the 1907 Traction Ordinances, and (B) in Releasing the City of Chicago and the Transit Authority from the Contractual Obligations Thereunder.

Section 23 of the 1907 Traction Ordinances (quoted in the margin, foot note 2, *ante*) provided that in case the City should designate a licensee to purchase the property after February 1, 1927, or should grant an ordinance to "another company" to operate, then the purchase of the properties must be made at the ordinance purchase price.

This provision was of course intended for the protection of the City against an exorbitant price in case of a municipal purchase after the expiration of the franchise quite as certainly as was intended to protect the companies against a confiscatory expropriation of their properties.

It is not disputed that as of January 31, 1946, such purchase price would amount to $172,133,759.10. (Tr. Auth. Ex. 73.) It is not disputed that this price, together with cash and other free assets of the company that would not pass by a purchase under the ordinances, would be sufficient to retire the Series B bonds in full as to the principal amount.

The City granted to the Transit Authority a franchise ordinance dated April 23, 1945. It was conceded that the

Transit Authority was a permittee or licensee of the City. As will be considered, *post,* the Transit Authority is in law "another company" as contemplated by Section 23 of the 1907 ordinance.

The 1907 ordinance was held constitutional in *Venner* v. *Chicago City Railway Co.,* 236 Ill. 349, and *Venner* v. *Chicago City Railway Co.,* 200 Fed. 1023, affirming the District Court's opinion in 195 Fed. 788.

In *Harris Trust and Savings Bank* v. *Chicago Railways Co.,* 39 Fed. (2d) 958 (District Court, July 16, 1929), to which case the City of Chicago was a party, as were the trustees under the first mortgage and the consolidated mortgage, the Court held that the purpose of the ordinance purchase price provisions was "to provide assurance, legally obligatory on the City, for the protection of the investment 'at and after' as well as 'during' the term expiring February 1, 1927. (pp. 960, 967.)"

Since this decision represented an adjudication upon the precise point in litigation to which both the debtor and the City were parties, it is *res judicata* upon the question of the intent and effect of the ordinance if that question coud otherwise be deemed doubtful, which we submit it could not. *Venner* v. *Chicago City Railway Company,* 236 Ill. 349, to which the City was also a party, is likewise *res judicata* on the point. (See *Grubb* v. *Public Service Commission,* 281 U. S. 470, holding specifically that where the right of the utility to operate under a grant might have been litigated in a previous state court proceeding, but was not litigated, the judgment of the state court was *res judicata* in the Federal Courts.)

Petitioners contended below and seek to urge before this court that the Metropolitan Transit Authority Act and the ordinance from the City to the Transit Authority, if

valid, give (as they must do) full recognition to the 1907 ordinance contracts. That this is true clearly appears from the following observations and authorities:

(1) The Transit Authority Act makes no reference to the 1907 ordinances. Neither that act nor the companion acts purport to amend, modify or repeal either the Mueller Act, or even Section 6 of Article 49, Chapter 24 (Cities and Villages Act) 1945 Illinois Revised Statutes, which carries forward the provisions of the Mueller Act pertinent here.[9]

(2) One of the companion acts to the Transit Authority Act, Article 23.28-1 of said Chapter 24, requires the granting of any ordinance by the City of Chicago to the Transit Authority before the latter may proceed with an attempt to do anything under its statutory authorization. Now it is significant that Section 23.28-1 provides that any such ordinance may be exclusive but makes the rights of the Transit Authority "subject to unexpired franchise ordinances * * *" This latter condition and restriction can only be construed to mean that the legislature was aware of the Mueller Act, the 1907 Ordinances and Section 23 thereof, the decisions and legal concepts presented above

[9] Sec. 49-6 of Chapter 24, 1945 Illinois Revised Statutes reads as follows:

"Sec. 49-6. RESERVATION OF RIGHTS IN FRANCHISE. It is lawful for any municipality to incorporate in any grant to a public utility company reservation of the right on the part of the municipality to take over all or any part of the property, plant, or equipment used in the operation of that public utility company, at or before the expiration of the grant, upon such terms and conditions as may be provided in the grant. It is also lawful to provide in any such grant that if such a reserved right is not exercised by the municipality, and if the municipality grants the right to another person to operate a utility in the streets and parts of streets occupied by its grantee under the former grant, the new grantee shall purchase and take over the property located in those streets and parts of streets upon the terms which the municipality might have taken it over."

in this brief. The provisions of Section 23, 28-1 embody a condition annexed to the grant of any ordinance to the Transit Authority.[10]

In the Statement in the Case, *ante,* we have explained how the City not only invited but insisted upon large reinvestments and new investments of additional capital increasing the invested capital from approximately $53-000,000 in 1907 to $172,000,000 as of January 31, 1946. These reinvestments and new investments were made upon the faith of the Traction Ordinances and the purchase

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[10] The question of the rights of the public utility under Illinois law to operate within the field by it developed has been determined and reaffirmed numerous times by the Supreme Court of the State of Illinois. In the recent case, **Chicago and West Towns Railways, Inc., et al., v. Illinois Commerce Commission, et al.,** Docket Number 29710—March 19, 1947 (unreported), there was presented to the court the power of the Illinois Commerce Commission to issue a certificate of convenience and necessity to Bluebird Coach Lines, Inc., to operate within the field theretofore occupied by Chicago and West Towns Railways, Inc. The Court held in part:

> "We pointed out in our former opinion that the appellee contended in effect that the day of regulated monopoly for utilities was a thing of the past, but in opposition to their views we specifically held, in accordance with our prior decisions, that the method of regulation of public utilities in force in Illinois is based upon the theory of a regulated monopoly rather than competition, and before one utility is permitted to take the business of another already in the field, it is but a matter of fairness and justice that it be shown the new utility is in a position to render better service to the public than the one already in the field, and that the power of the State to regulate a utility carries with it the power to protect such utility against indiscriminate competition, and that such power should be exercised to that end. **West Suburban Transportation Co. v. Chicago & West Towns Railway Co.,** 309 Ill. 87; **Chicago & West Towns Railways, Inc. v. Illinois Commerce Commission,** 383 Ill. 20.
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> "In our former opinion we said: 'Upon the showing made in the record, the commerce commission was without authority to issue a certificate of convenience and necessity to the Bluebird line. Before it may do so it must be established that appellants, as pioneers in the field, are unable to adequately perform the service which may be found necessary or convenient by the commerce commission.' The order and finding of the commerce commission as a matter of law does not establish that appellants are unable to adequately perform the services offered by the Bluebird Lines, but on the contrary do show that appellants are fully able and willing to perform the same or better service."

price provisions in Section 23 thereof.[11] The City and its privy, the Transit Authority, are therefore clearly estopped to assail either the validity or the intention of the purchase provisions. (See *Pierce* v. *Somerset Railway,* 171 U.S. 641, holding that the validity of state legislation authorizing a railroad reorganization cannot be questioned by those benefitting from the reorganization even on the ground that the statute is unconstitutional, the doctrine of estoppel applying. See also *People* v. *Vaughan,* 282 Ill. 163, declaring that "an estoppel may * * * prevent the assertion of a constitutional right." See also

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[11] The Illinois Commerce Commission has construed Section 23 of the ordinance as being in force. In case No. 30895 (May 3, 1943—rate case) the Commission stated, in part:

> * * * "Those Settlement Ordinances specified in detail certain methods which were to be followed in the capital and expense accounting practices of petitioners. The ordinances further provided for currently maintaining, under the supervision of the Board, an up-to-date figure designated in the ordinance as 'City Purchase Price.' This 'City Purchase Price' fulfilled a dual function in the succeeding regulation of the Chicago Surface Lines and its relations with the car riders and the City of Chicago. These two functions of the 'City Purchase Price' were (1) to establish a standard property valuation upon which an allowed return of 5 per cent would be computed before an allocation was made of remaining net revenues over the 5 per cent between the City (55 per cent) and the corporations (45 per cent); and (2) it established a price at which, under ordinance provisions, the City of Chicago would be permitted to acquire the properties of the corporations in the event that the City elected to engage in the operation of the Chicago local transportation system. **The ordinance further provided for the contingency that at the expiration of the franchise a new franchise might not be immediately effective, and in essence provided for a continuation of these particular provisions until such time as a superseding ordinance might be in effect or the City consummated its purchase of the properties."** (Emphasis supplied.) 22 Ill. Commerce Commission Opinions and Orders (Ill. C. C.) 683.

The trustees of Chicago Railways Company asserted before the District Court their position with respect to Section 23 of the 1907 ordinance, in their answer to the claim of the City of Chicago for compensation, etc., as follows:

> "The use of the City streets by the receivers of the debtor, during the period in question, was pursuant to the ordinance of February 11, 1907 to Chicago Railways Company, which constitutes the contract between the City and said debtor covering the use of the city streets. The ordinance of February 11, 1907, contemplates a continuance of the debtor's franchises and the right to use the city streets after February 1, 1927, until the railway system is purchased and taken over by the City or its licensee. * * *" (Tr. 2663, p. 2.)

People v. *City of Rock Island*, 215 Ill. 488, 75 N.E. 437, holding that a City is estopped to assail the validity of a grant to a public utility of rights of way in a public street after the public utility has invested capital and the city has profited by such investment.)

The District Court did not decide the questions raised by these contentions adversely to Petitioners. It did not decide them at all. The District Court and the Circuit Court gave no consideration to the ordinance purchase price.

On the contrary, the lower courts treated the question of the right of the companies to occupy the city's streets as "doubtful," expressly gave effect to alleged judicial "doubts" as to such rights as debasing the value of the companies' properties as thus debased as a basis for finding that Petitioners had no equity in the debtor's estate. Thus the District Court used its "doubts" to depress "value" and then used "value" as thus depressed to find that Petitioners had no equity in the debtor's estate.[12]

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[12] Opinion February 15, 1946 and entered February 20, 1946. (Tr. 3461, pps. 4-6.)

"In arriving at the sales value of the portion of Chicago Surface Lines assets here proposed to be sold to the Authority, a not over-optimistic buyer might justifiably find considerable uncertainties or risks in the followng facts or assumptions:

"That the 20-year period mentioned in the 1907 franchise ordinances expire in 1927 and that the City contends that the company's occupancy of the streets is at sufferance rather than of right;

"That the Chicago Transit Authority is in existence with the support and blessing of the City and State;

"That the Authority is a municipal corporation with the power of eminent domain and with the right to operate tax free, and that the City has actually granted an exclusive franchise to the Authority;

"That the Authority, if this plan fails, may in cooperation with the City of Chicago install competing bus lines on the principal revenue-earning lines of the companies and bring the companies into a financial crisis similar to that in which the privately owned companies in San Francisco found themselves in the face of municipal competition (see Market Street Ry v. R. R. Commission, 324 U. S. 548);

The Circuit Court of Appeals, acceding to this reasoning on the part of the District Court, reasoned further that the companies' rights in the City's streets, if any such rights they had, were assets of the companies which might be sold or relinquished precisely as might any other intangible right of a corporate debtor undergoing liquidation in bankruptcy. (Decision, p. 12).

But both the District Court and the Circuit Court of Appeals overlooked the fact that to permit alleged doubts of the court, or the putative doubts of a hypothetical purchaser, as to these rights, to depress the value of the properties, when the District Court could and should have defined and determined these rights, was not only improperly to debase the *valuation* of the properties, but was in effect a refusal *even to define or determine the nature of the property rights that the court was undertaking to sell.*

Petitioners say that when a court does not even decide what property it is proposing to sell, although all of the parties whose presence is necessary to such a determination are before it, the Court has no possible or conceivable basis for holding that junior security holders are pretermitted from participation in the plan *because of the low valuation placed upon the properties by the Court on account of these unresolved doubts.*

Petitioners contend that the ordinance purchase price represents the minimum figure at which the City (or the Transit Authority, as its licensee and privy) can acquire

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"That the absence of a franchise to the Chicago Surface Lines and the possession of an exclusive franchise by the Authority and the latter's actual use of that franchise, may give rise to a contention and possibly a holding that the properties of the Chicago Surface Lines Companies are to be valued as junk, under a possible application of Mr. Justice Holmes' dissent in Denver v. Denver Union Water Co., 246 U. S. 178, 195;"

the properties of the debtor without the consent of the Series B bondholders. The other evidence and considerations of value considered post are without prejudice to this point.

This court's rule 52 (a) requires that the District Court "find the facts specially and state separately its conclusions of law thereon."

The District Court's recitals, pronouncements and observations deal with such jurisdictionally vital matters as "valuation," fairness, equitability, and feasibility. But inasmuch as these pronouncements, recitals, and conclusions are *admittedly* based upon the District Court's failure to define the rights of the debtors in Chicago streets and to rule upon Petitioners' contract rights under the 1907 Ordinances in the indenture securing their bonds, *such pronouncements cannot possibly constitute findings at all.* It is therefore with the greatest earnestness that Petitioners argue that the District Court order should be reversed if for no other reason than that it does not embody findings which will enable this court understandably to review it.

These infirmities, we submit, similarly vitiate the other pronouncements of the court discussed hereafter.

II.

The District Court Impaired the Obligation of the Series B Bondholders' Contracts with Senior Security Holders and the City, Which Contracts Were Neither Assets Nor Liabilities of the Debtor Companies and Were Not Subject to the Court's jurisdiction.

The covenants in the Consolidated Mortgage securing the Series A and Series B bonds constituted a contract among the bondholders that the City's obligation to pay the ordinance purchase price for the debtor's properties

in the event that they were ever taken for municipal use or by "another company" should never be impaired. This contract constituted a promise among the security holders *inter sese*. The City assented to and is bound by this contract; for, as we have shown, it invited and required the reinvestment in the securities of the debtor as well as investment in the system of earnings upon which the bondholders had a lien under their mortgage.

These contractual rights among the security holders *inter sese* were not an asset of the debtor. Therefore, they could not be sold incidentally to the liquidation of the debtor's estate. They were not an obligation or liability of the debtor. Therefore they could not be discharged or compromised incidentally to a disposition of the debtor's estate.

The Circuit Court of Appeals recognized that, in that court's language, quoted *ante*,

> "Section 23 does provide that if, after the expiration of the ordinance, the City should grant a franchise to a new company, the new company shall buy the property upon the terms upon which the City might have purchased."

But the Circuit Court of Appeals held that

> "Even so, that fact, under the circumstances in this case, is no reason why the plan should not be approved, since all contingent rights of a debtor pass to its trustees and become part of its estate, *Pollack* v. *Meyer Bros. Drug Co.*, 233 F. 861, and may be dealt with in Chapter X proceedings."

But the Circuit Court of Appeals ignores the fact that the rights claimed by the Series B bondholders are (a) not contingent and (b) are vested in the Series B bondholders and not in the debtor or their trustees. These

rights subsist directly between the Series B bondholders and the City and Transit Authority and are neither assets nor liabilities of the debtors.

Yet neither the District Court nor the Circuit Court of Appeals would even pass upon, much less sustain, this very substantial claim of right asserted by Petitioners. On the contrary, the District Court and the Circuit Court approved the plan which requires under Section G that all rights under the ordinance be released by the trustees to the City of Chicago.

Pollack v. *Meyer Bros. Drug Co.*, 233 F. 861, which is the only case cited by the Circuit Court of Appeals in thus disposing of without adjudicating Petitioners rights, holds merely that a remainder of the bankrupt under a certain trust passed to his trustee in bankruptcy even though there was a division of opinion as to whether the remainder was vested or contingent.

Petitioners concede that the Series A bondholders' *lien upon the physical assets only* is superior to that of the Series B bondholders. But the contract that a licensee of the City (or its privy or the grantee of a new ordinance franchise) would be obligated to pay the ordinance purchase price for the properties is not a lien or a mortgage upon the estate of the debtor. It is a contractual engagement upon the faith of which the present system was largely built by invested private capital.

In Remington on Bankruptcy (5th Edition), Sec. 4395, it is stated as follows:

> "The grant of jurisdiction for the purpose of corporate reorganization under Chapter X is not to be construed as giving jurisdiction to administer the

> property and affairs of others than the debtor; thus, not to administer property that is in the debtor's possession as a trustee nor to adjudicate its rights and duties as such fiduciary."

The rights under Section 23 of the Ordinance are also common rights among the Series B bondholders (and also among all junior security holders) and the Court is without jurisdiction to release or cause to be released to the City or Transit Authority rights under the Traction Ordinance.

The Court is without jurisdiction to give effect to Article II G of the plan (Tr. 3231 p. 22) requiring the trustees to waive, release and discharge all rights under the Traction Ordinances and property in said Section G stated. *In re Diversey Bldg. Corporation* 86 F. (2) 456 (C.C.A. 7th) (1936) it was held that a guarantor could not be released as against non-assenting bondholders in consideration of his guaranty of new bonds under the plan.

Chapter X of the Bankruptcy Act was certainly never intended to afford a means whereby the senior security holders, the City, and the Transit Authority, none of whom is in bankruptcy, could escape the force of their own contractual obligations.[13] Certainly Section 216 (10), upon which the District Court relied, enacts no means whereby the City or the Transit Authority may escape contractual obligations running directly to the Series B bondholders.

[13] Even if it should be supposed that the Series A bondholders did not contract with the Series B bondholders the Series B bondholders have a direct and immediate contractual obligation of the City, arising out of the fact that of their investment and reinvestment in the companies on the faith of the promise uttered in the ordinance, that the City would never preempt their properties except in accordance with Section 23 of the ordinance.

III.

The District Court Erred in Refusing to Project Prospective Earnings on the Basis of a Ten-Cent Basic Fare.

As we have explained in the Statement to the Petition, *ante*, the District Court found that the debtors were entitled to a ten-cent basic fare. It authorized its trustees to apply to the Illinois Commerce Commission for an increase in the present eight cent to such ten-cent basic fare. Such petition is now pending before the Commission.

But the District Court refused either to assume that the Commission would grant the fare to which the District Court thought the debtors entitled or to await the actual outcome of the application to the Commission for such increase in fare. On the contrary, although the District Court professed to adopt "capitalization of prospective earnings" as its basic criterion for valuation, it projected earnings on the basis of the present eight-cent fare. Such projected earnings were $4,000,000, which were the net earnings for the fiscal year ended January 31, 1946. (Trans. Auth. Ex. 73).

The record discloses (P.T. 1023-29) that the ten-cent fare prevails in many of the principal cities.[14] It is not disputed that the ten-cent fare prevails in the City of Chicago for motor bus transportation rendered by Chicago Motor Coach Company.

The petition authorized by the court contemplates and, unless the schedule is affirmatively disallowed by the commissions, will result in an increase of two cents per adult

[14] Subsequent to the decision of this court in **Market Street Ry. v. Railroad Commission of California**, 324 U. S. 548, and the acquisition by the City and County of San Francisco of the Market Street Railway System the basic rate of fare for the City and County of San Francisco Municipal System was increased to ten cents. (P. T. 1023-24) American Transit Association—Passenger Transport. Vol. 3, No. 34 (p. 1) January 4, 1946.

passenger and upward adjustments for other persons. It has been assumed by all concerned that this increase would result in additional revenue of approximately $14,000,000 a year. (P.T. 1039). Added to the court's $4,000,000, this would bring earnings (so far as shown by the record) to $18,000,000 a year. From this sum, however, must be deducted approximately $8,000,000 to cover a recent wage increase. (Trans. Auth. Ex. 74.) Therefore this increase would leave net earnings of approximately $10,000,000. Even capitalized at the high figure of a 7% rate, and without regard to other criticisms of the court's valuation, this would bring the capitalized value of the properties to approximately $135,000,000, a figure that excludes free cash and other assets owned by the company which would be transferred under the plan and upon which the court does not find a value.

By its orders in the recent rate case proceedings,[18] the Illinois Commission has found a rate base of a least $128,000,000, and an original cost depreciated value of the public utility property of more than that figure. (22 Ill. C.C. 690). *The Illinois Public Utilities Act and law commands the commission to allow a fair return on fair value of property.*[19] That Commission in its temporary orders on

[18] May 3, 1943.

[19] A rate to be reasonable must be so to both utility and the public. To the consumer it is "a rate somewhat less than the full value of the service to him * * * but not more than the services are reasonably worth," and to the utility it is "a rate above the point at which it would become confiscatory; * * * to induce the investment * * * of capital there must be some hope of gain commensurate with that realizable in other businesses, and the mere assurance that the investment would not be confiscated would not suffice. * * *" Public Utilities Commission v. Springfield Gas Co., 291 Ill. 209.

The Supreme Court of Illinois has further announced "a rate that is confiscatory or insufficient to pay costs of the traffics and other proper outlays for taxes, etc., and to return to the carrier a reasonable profit on the investment, infringes upon the constitutional rights of

April 10, 1942, allowed an increase of one cent in rates, which was all that was prayed for, and found that even on an eight-cent fare, on the basis of the facts then existing, there would be net earnings of $7,500,000 annually, on a tentative original cost of at least $128,000,000 (22 Ill. C.C., page 688, 690, finding 4).

In other words, the District Court found that the System would be entitled to an increase in revenue which would support a valuation admitting Series B bondholders to participation in a reorganization, evidently assumed that the Commission would fail to do what the Court thought would be its duty to do, namely, grant that increase, refused to see whether the assumption of future

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the carriers by depriving it of property without due process of law and is void, whether fixed by the statute itself or by the commission." **Public Utilities Commission v. Chicago & West Towns Ry.**, 275 Ill. 555, 568.

In the case of **Peoples Gas Light Co. v. Slattery**, (1940) 373 Ill. 31, speaking through Justice Gunn, the court stated at p. 53:

> "The valuation of the property of the company was ascertained by the commission considering the present value of the real estate, the reproduction cost new of the structures and equipment, the original or historical cost, and included in the valuation was the sum of $7,500,000 for working capital and the sum of $7,200,000 for any intangible or other elements of value which may not have otherwise been provided for, which would, of course, include going value. The elements considered by the commission were proper elements to be taken into consideration in the valuation of the utility for rate-making purposes or in confiscation cases."

On page 54 the court quoted with approval that portion of its decision in the case of Public Utilities Commission v. Springfield Gas and Electric Co., 291 Ill. 209, reading as follows:

> " 'The basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a public utility under legislative sanction must be the fair value of the property being used by it for the convenience of the public, and in order to ascertain that value the original cost of construction, the amount expended in permanent improvements, the present cost of construction, the probable earning capacity of the property under the particular rates prescribed by statute, and the sum required to meet operating expenses are all matters for consideration and are to be given such weight as may be just and right in each case.' This proposition is supported by the great weight of authority."

dereliction on the part of the Commission was well founded by awaiting the event of action on the application that the Court authorized and directed, and, after sustaining the burden of these proceedings for many years, suddenly conducted them so expeditiously that there was not even time to see whether the Commission would act as the Court thought that it should.

Had the District Court projected earnings upon the basis of the ten-cent fare to which it found the companies to be entitled, the properties would have sustained a valuation which would have admitted the Series B bondholders to participation in any reorganization or in th eproceeds of any sale at such valuation.

Petitioners maintain that for this reason alone, *certiorari* should be granted.

IV.

The District Court's Valuation of the Debtor's Properties, Upon Which Valuation the Propriety of Excluding Series B Bondholders from the Plan Depends, Does Not Respond to Juridical Concepts of Value.

A.

The District Court treated Transit Authority's offer as evidence of the maximum value of the property, thereby allowing such offer to justify itself.

It should be observed at the outset of any consideration of the lower court's valuation that, aside from the fact that it debased the valuation of the debtor's properties by doubts which it could or should have resolved, and achieved its valuation by supposed projected earnings on an eight-cent fare basis instead of a ten-cent fare basis, it stated frankly in its opinion that the Transit Authority

was in existence "with the blessing" of the City and the State and was so prepotent a prospective bidder that no one could bid against the Authority at a fairly competitive auction.

The District Court then reasoned that the Transit Authority's "negotiated offer" (as the Court calls the present plan) effectively freezes competitive bidding. Indeed, the District Court lays heavy emphasis upon the present plan as the result of "negotiations" on the part of the Transit Authority for the acquisition of the debtor's properties. To put the matter another way: The Court used the Authority's non-competitive "price" to appraise "value" and then used the "value" as thus found to justify the "price."

Stated in the simplest possible terms, the District Court's finding of value was admittedly based upon the pressure or leverage exered by the Transit Authority in "negotiating" for the properties. The District Court candidly says as much; for the District Court observes that "a not-overoptimistic buyer might justifiably find considerable uncertainties or risks" in the fact that "the Chicago Transit Authority is in existence with the support and blessing of the City and State" and "is a municipal corporation with the power of eminent domain and with the right to operate tax free, and that the City has actually granted an exclusive francise to the Authority." (Footnote 12, *ante*).

Then the District Court exploits the Transit Authority's unwillingness to pay more than $75,000,000 for the property as overt evidence, consisting of a concrete offer, supporting the Court's finding that the property is not worth more than that figure. (Tr. 3461, p. 8).

It is thus apparent that, the District Court's declara-

tion to the contrary notwithstanding, the figure of $75,000,000 represents anything but a "negotiated value." *(See Statement of Friedman and Tenney, counsel for the first mortgage bondholders, P.T. 252 stating that "as long as the first mortgage bondholders are being offered par, they have no interest in any testimony offered as to value * *.")*

Petitioners submit that any such method of "valuation" as this so clearly violates both the Federal and State Constitutional inhibitions against the taking of private property for public use without just compensation as to render the Court's *fiat* of value not responsive to the juridical concepts implied by that term and therefore invalid as a matter of law.

Further to demonstrate the infirmities of the District Court's methodology of valuation, we may call the court's attention to the fact that a serious contest arose as to the validity of certain claims on the part of the City for alleged compensaion and other miscellaneous items. Petitioners vigorously resisted these claims on the ground that the City had not rendered the services in respect of which they were asserted and was not entitled in law to any compensation in the premises. We do not ask this court to decide that these claims were either valid or invalid. But we do emphasize that the District Court refused to pass upon the validity of these claims and by refusing to determine their validity treated the claims as being matters subject to negotiation and settlement in connection with the purported justification for the provisions in the plan (a) requiring the release to the City of all the rights under the 1907 Ordinances, and (b), the release of the trustees' claim against the City of $5,750,000, which last claim was the subject matter of litigation in the Circuit Court of Cook County (Article II-G-plan).

This refusal to adjudicate these claims was important because it evinces the District Court's propensity to depress the value of the properties by doubts that the Court should have resolved. The basis for these claims, if it is valid at all, would persist in the future in the event of continued private ownership of the properties. Therefore, it was of the utmost importance that the validity or invalidity of these claims of the City be determined since the amount to be paid to the City would affect the companies' earnings and it was upon the basis of earnings that the Court undertook to find value.

B.

The Securities and Exchange Commission's valuation, when reconstructed to allow for (a) a ten-cent fare, (b) resolution of doubts as to the companies' rights in the streets, (c) reorganization of the Surface Lines without the Elevated Lines, and (d) effects of a modernization program, supports a valuation admitting Series B bondholders to participate in distribution.

The District Court thought that it found support for its $75,000,000 valuation in the advisory reports of the Securities and Exchange Commission. (Tr. 3461, p. 6.) That figure was indeed pronounced by that Commission. But at the time that the Commission made its pronouncement, it was considering a hypothetical plan for the integration of the Surface Lines with the Chicago Transit System, $75,000,000 representing the Commission's allocation to the Surface Lines of their share of the total hypothetical price. The Commission also assumed an eight-cent fare. And the Commission expressly stated that it used a 7% factor in capitalizing earnings instead of a lower figure because of the Commission's doubts as to the companies' rights in the city streets.

But the fact is that the Elevated Lines of the Rapid Transit System have long been losing money. Therefore, although their integration with the Surface Lines would increase the capital investment represented in the integrated system, it would decrease potential earnings; for profits of the Surface Lines would be in part absorbed by losses of the Elevated Lines. Therefore, an allocation to the Surface Lines of a percentage of the value of the total hypothetical integrated system, when capitalization of earnings and not investment of capital is the basis of valuation, would depress rather than enhance the value of the hypothetical entirety.

It is obvious from studies in the record (P.T. 1050-1081; Pet. Exhs. 36-40; P.T. 1055, 1065, 1066, 1067, 1070, 1080) that even without other adjustments of the Securities and Exchange Commission's valuation, as stated in its Advisory Opinion, exclusion of the Elevated Lines from the reorganization would afford a valuation of at least $123,000,000. The infirmities observed by the SEC in its determination of value based on capitalization of earnings of the combined properties were cogently presented by Dr. Guthman, Department of Accounting and Finance, Northwestern University (P.T. 1090, 1094-99).

In its Supplemental Report of February 8, 1946, the SEC considered the Surface Lines valuation independent of the Rapid Transit System. (Tr. 3433) It found $7,000,000 as probable earnings after modernization (Tr. 3433, P. 14); but applied an allegedly high rate of capitalization because of the allegedly undecided ordinance question that in concluded $75,000,000 to be a fair price. (Tr. 3433, pp. 15-16).

The Securities and Exchange Commission may be excused for using a high capitalization factor on account of

its uncertainties as to the companies' rights in the city's streets. That Commission had no jurisdiction to resolve such doubts and could only place itself in the position of a hypothetical purchaser. But the District Court, unlike the Commission, could and should have resolved these doubts. (See Point I, *ante*.) Had it done so, and had it then desired actually to follow the principles of the Securities and Exchange Commission's valuation, it would have had to reduce the capitalization factor because the Commission's high figure was expressly predicated upon these unresolved doubts. Had it applied a 7% rate of capitalization to the $7,000,000 a capitalized value of $100,000,000 would result, to which would have been added free cash, non-utility property and other assets. Had the Securities and Exchange Commission reduced this figure from 7 to 5½%, the valuation of the Court without any other adjustments of the Commission's formula would have given a capitalized value of at least $125,000,000.

The Securities and Exchange Commission, not having control of the debtor's funds, was not in position to contemplate the full modernization program and the economies that were certain to result therefrom, but as stated *ante*, the SEC allowed $7,000,000 as probable earnings after modernization and on the basis of the eight-cent fare.

Finally, the Commission projected earnings upon the basis of an eight-cent and not a ten-cent fare. If its formula is used with a ten-cent instead of an eight-cent basic fare, then, even without other corrections, the value of the properties would have been substantially larger.

We know of no instance in recent periods where public financing has been made (or permitted by the Securities and Exchange Commission) in an amount equal to the full

fair value of the property to be acquired. *This factor alone indicates that the property has a value in excess of that found.*

We do not ask this court to revise or even review the formula used by the Securities and Exchange Commission On the contrary, we ask this court to take cognizance of the fact that if that formula is applied to the *data* that were before the court but not before the Commission, namely, separate operation of the Surface Lines, resolution of doubts as to the utilities' rights in the streets, projected effect of a ten-cent fare, economies certain to ensue from full modernization, and separate reorganization of the debtors without the Elevated Lines, the Commission's formula supports the petitioners and not the court.

C.

A Prior Finding of Approximately $136,000,000 as a "Valuation of the Properties for Reorganization Purposes" Affords a Minimum Basic Figure in This Case, to Which Figure Must Be Added other Assets Some of Which Were Not Evaluated by the Court.

On November 27, 1941, the court had before it a proposed plan of unification of all of the surface lines companies properties with those of the Rapid Transit System under a contemplated reorganization. The District Court made extensive and detailed findings under the caption "Valuation Findings." The court said in these findings:

> "The draft of order which reflects an aggregate value of $179,348,467.57 is approved by the court and will be entered." (Pet. Appx. 269.)

Of this amount, the District Court allocated 24% to the Rapid Transit properties and 76% to the Surface Lines properties.

In the subsequent order entered February 19, 1942, which order tentativey approved the plan last mentioned, the District Court reiterated this finding and speaks of the "total of $136,329,674.57 found" as the "value of all of the assets of the Surface Lines." (Pet. Appx. p. 287, 288.)

The orders embodying these findings have never been appealed from. However, this valuation reflected a depressed value of the Surface Lines because of factors involving Unification with the Rapid Transit System.

It is the position of Petitioners that "valuation for reorganization purposes" was a material and important issue before the court, with respect to which all interested parties had a right to be heard, and that this finding that on the dates of the orders last mentioned, respectively, the figure $136,329,674.57 was the least possible value of the Surface Lines properties for reorganization purposes although determined on the basis of unification and its depressing influence on the value of the Surface Lines properties.

Petitioners concede that in 1946, it would have been competent for the court to consider any legitimate additions to or subtractions from the property, or other incidental changes in value due to factors occurring in the efflux of time between the prior orders and the 1946 order. But it is not found or suggested by the court, nor was it claimed in the record by any interested party, that the value of the properties has shrunk between 1942 and 1946 by anything like $61,329,674.57, which represents the difference between the 1942 valuation and the 1946 valuation. In fact, no evidence was taken upon the question in changes of reorganiaztion value between 1942 and 1946, as such. But the record discloses evidence, considered *post*, that the reorganization value of the Surface Line properties should be larger than found in 1942.

Let us suppose that these findings were not *res judicata*. This court's reading of the findings and the District Court's reasoning supporting the 1941 valuation will convince it, we believe, that the valuation was a fair and a sound one. How, then, can it be "fair and equitable" to sell these same properties in 1946 for $75,000,000 with no explanation or even intimation for this drastic and (we are forced to argue, *post*) wholly unsubstantiated reduction in value?

The plan contemplates the taking of privately owned property for public use under municipal ownership. The fact that the taking is proposed to be accomplished through the mediacy of bankruptcy proceedings rather than through the usual processes of eminent domain does not mean or suggest that the private property may be taken for the public use without just compensation. In the margin we note those factors which, under the applicable Illinois law of eminent domain (which limits the powers of the Transit Authority even though it proposes to purchase through the Federal Court rather than the state courts) would have to be taken into account in determining just compensation.[16] [17]

[16] The respondent committees stated what the Petitioners conceive to be certain basic concepts applicable in the determination of reorganization or eminent domain value in their joint memorandum filed with the District Court in 1941 (Pet. Appx. 253-66) which reads in part:

> * * * "Among the 'valuations for other purposes' which 'indirectly bear on earning capacity' in the case of a public utility, such as a local transportation system, is its value for ratemaking purposes. Since its rates are regulated on the principle that it is entitled to earn a fair return on the fair value of its property, it is important that consideration be given to the factors from which such fair value is determined. If no consideration were given to these factors of ratemaking value, the reorganization value might exceed the value upon which the new company would be entitled to earn and thus security holders not warranted in participating in the reorganization would, in fact, participate. And, conversely, if the estimated earnings capitalized at a fair rate did not produce a valuation as high as the rate-making value, the court would be warranted in giving some weight to the latter valuation if it believed that the utility might earn a reasonable return on such a rate base.
>
> "It is for the above reasons that the elements upon which rate-

Even if capitalization of prospective earnings be adopted as the sole criterion of value, these factors are nevertheless relevant because under the Illinois law, the Illinois Commerce Commission would have to give effect to them in fixing the earnings which are to be capitalized.

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[16] Continued
making value is based, such as original cost, reproduction cost and reproduction cost less depreciation are factors to be considered in a public utility reorganization proceeding. The foregoing factors have been considered in all of the railroad reorganization cases of the Interstate Commerce Commission discussed in the memorandum previously submitted to the court as Exhibit 1A and also in some of the utility reorganization cases of the Securities and Exchange Commission (West Ohio Gas Case, 3 S. E. C. 1014; Derby Gas Case, Public Utility H. C. A. Release 2875; United Power & Light, 5 S. E. C. 483.)"

[17] The following elements of value appear in the record:

Values determined by Illinois Commerce Commission in its 1942-43 rate case (22 Ill. C. C. 690):

Original cost—more	$128,000,000.00*
Original cost depreciated—at least	128,000,000.00*
Original Cost Depreciated, Utility property, (as at June 30, 1942) approximately (P. T. 833-34)	144,475,350.00**
Reproduction cost, new (1942) (Utility property) (P. T. 1038)	267,341,235.00**
Reproduction cost, new, depreciated (1942) (Utility property) (P. T. 1038)	178,662,231.00**

Court valuation:

District Court, in connection with the 1941-1942 reorganization plan, valued the Surface Lines property at (round figures)	136,000,000.00**

The following further evidence of value appears of record as to the property as an entirety involved in the instant proposal:

	Surface Lines System	Chicago Railways Company
Reproduction cost new, as at June 30, 1941	$288,947,128.00	$171,762,875.00***
Reproduction cost new, depreciated, as at June 30, 1941	209,528,813.00	121,226,978.00***
Original cost, as at January 31, 1941	176,013,817.08	104,312,113.37****

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*To these several figures there would be added the value of the non utility property, free cash assets of approximately $18,000,000 and other free assets including the value of claims against the City of Chicago.

**To these figures there would be added said free cash assets of approximately $18,000,000, the value of the non-utility property, and the value of claims against the City.

***Chicago Surface Lines Exhibit 41, (P. T. 46, 50-51).

****Chicago Surface Lines Exhibit 37, (P. T. 32, 33, 36).

Inasmuch as the net result of this plan, if it should be consummated, would be the acquisition by public authority of private property for public use within the purview both of the Fifth and Fourteenth Amendments to the Constitution of the United States and of the Illinois Constitutional and statutory provisions pertinent in eminent domain proceedings, Petitioners maintain that if such acquisition could be accomplished at all through Chapter X proceedings, the principles of eminent domain must, if Petitioners constitutional rights are to be respected, be given effect. we cite as pertinent the following authorities, which deal with the acquisition of public utility properties by eminent domain: *Appleton Water Works Co.* v. *Railroad Commission,* 154 Wis. 121; 142 N.W. 476, 47 L.R.A. (N.S.) 770; *Oshkosh Water Works Co.* v. *Railroad Commission,* 161 Wis. 122, 152 N.W. 859; L.R.A. 1916 F 592; *Kennebec Water District* v. *City of Waterville,* 97 Maine 185, 54 Atl. 6, 60 L.R.A. 856.

There is another reason, wholly apart from the fact that the Transit Authority's offer was found by the Court to be virtually coercive, why it was not a "negotiated offer." *It was not "negotiated" with the owners of the property. The Court's trustees did not consent to the plan.* The senior security holders were not "owners." Petitioners were not consulted during the negotiations. Should it be argued that Petitioners had no equity in the properties and were not consulted for that reason, the reply is that the District Court used its concept of "negotiated value" as a factor influencing its conclusion that the Series B bondholders had no equity in the property and then used its conclusion that the Series B bondholders had no equity in the property as precluding them from objecting to the plan.

The Fifth Amendment, we submit, clearly inhibits a Dis-

trict Court from sanctioning the preemption of privately owned property for public use upon a conception that a "negotiated value" dispensed with the necessity for consulting the principles of eminent domain when (a) the Court expressly recognizes that the threat of eminent domain is a factor depressing the "negotiated value" and (b) the alleged "negotiation" is not with the owners of the property.

The Fifth Amendment (which binds the Federal Courts) and the Fourteenth Amendment (which binds the state and its municipal corporations) concurrently required that the District Court recognize the ordinance purchase price as determining the value of the debtors' properties if they were to be taken for municipal use or under Section 23 of the ordinance. These same constitutional requirements should have constrained the District Court to render judgment instead of expressing unresolved doubts as to these very important matters.

This phase of the case is still at large and undecided and in and of itself should evoke this court's writ of *certiorari*.

Petitioners therefore submit that the District Court's order violates the Fifth Amendment to the United States Constitution and sanctions a violation by an Illinois municipal corporation of the Fourteenth Amendment.

D.

This court should not itself determine the valuation of the properties. It should remand the cause for redetermination by the District Court in accordance with proper principles.

We do not ask this court itself to undertake a revaluation of the debtor's properties. We are mindful of the

respect that this court very properly pays to the pronouncements of commissions and lower courts upon the complex legal, factual and economic problems of the valuation of public utilities and other vast properties *when the inferior tribunal has observed appropriate canons of valuation and has properly regarded due process.*

But the same principle of appellate jurisprudence that deters this court from making its own independent valuation requires it to see to it that the lower courts or commissions' valuation responds to appropriate juridical concepts of value. If this court cannot and lower courts do not properly undertake the problem of valuation, due process is clearly denied.

We submit that the District Court so far departed from the appropriate principles of public utility valuation that its figure of $75,000,000 is not responsive to the meaning of the term "value" as that term is used in bankruptcy jurisprudence. The figure therefore should be disregarded.

V.

The orders appealed from were not only erroneous but void because the trustees were not directed either to "file a plan or a report of reasons why a plan cannot be effected." Section 169 makes such a direction to trustees and compliance therewith prerequisite to the approval of any plan.

The language of Section 169 of Chapter X is clear, positive and mandatory. It is as follows:

> "Sec. 169. Where a trustee has been appointed the judge shall fix a time within which the trustee shall prepare and file a plan, or a report of his reasons why a plan cannot be effected, and shall fix a subsequent time for a hearing on such plan or report and for the

consideration of any objections which may be made or of such amendments or plan as may be proposed by the debtor or by any creditor or stockholder."

But notwithstanding the plain meaning of the language above quoted, the District Court never has directed the trustees to "file a plan or a report of reasons why a plan cannot be effected" for the Chicago Surface Lines properties; nor have the trustees filed a plan or reported reasons why a plan cannot be effected.[18]

It is urged that the instant debtor's properties would, in fact, be susceptible to a corporate reorganization, properly so called, and that therefore they should not be disposed of by sale and liquidation. But the point is distinct from the present point, which is that submission of a plan by the trustee (or a report setting forth "why a plan cannot be effected") is a categorical prerequisite to the jurisdiction of the court either to approve a plan not submitted by the trustee or to liquidate the debtor's properties. We submit here, as we submitted in connection with the requirement of Section 178 (post), that no resort either to legislative history or to other aids to statutory construction is necessary in order to read the plainly expressed will of Congress. But if there could otherwise be any uncertainty as to whether Congress meant what it said, that uncertainty

[18] Early in the Chapter X Proceedings, the District Court did instruct the trustees to undertake to formulate a plan for the unification of all of the Stree Car Company properies in Chicago and the Chicago Elevated Lines. A plan was developed, bearing the date November 29, 1944, contemplating enforced unification of the properties of the five Street Car Companies and the Elevated Lines, pursuant to the unification ordinance of the City of Chicago of June 19, 1941. But that plan was, of course, not one for the reorganization of the instant debtor within the purview of Chapter X. This plan was disapproved by the Illinois Commerce Commission by its order or report of June 5, 1945.

vanishes upon a reading of the excerpts of the legislative history quoted in the margin.[19]

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[19] EXCERPTS FROM THE HEARING BEFORE THE COMMITTEE ON THE JUDICIARY, HOUSE OF REPRESENTATIVES, SEVENTY-FIFTH CONGRESS, FIRST SESSION, ON H. R. 8046 (THE CHANDLER ACT).

"The bill prescribes new duties for the trustee, requiring a careful investigation into the acts, conduct, property, liabilities, financial conditions, etc., of the debtor; how its business was operated; the desirability of its continuance. He must report to the court on all facts that might pertain to misconduct or mismanagement. He must prepare a brief statement of his findings and transmit it to the creditors, stockholders, and other parties in interest. The Act will require statements at regular intervals. All plans for reorganization must be submitted to the trustee, who in turn, will present the plan or plans, which in his opinion are the best, to the court."

Mr. Chandler,
Opening Statement, House Committee Hearing page 5 (2).

* * * * *

"Now, the third function here is the assembling of the reorganization facts: Not only the facts as to the claims running to the estate, not only the facts as to the competency and the faithfulness of the management; but also the financial and business facts that are the necessary ingredients of any plan of reorganization. That third matter becomes important in view of the second function which this independent trustee under the Chandler bill would perform, and that is this—Mr. Weinstein just touched on it, and I will elaborate on it for the purpose of a clear understanding: Under the Chandler bill the independent trustees would be the formulator, so to speak, of the plan of reorganization. Any securityholder, creditor, or stockholder could submit to him his ideas as to what should go into the plan, or he could submit to him a full-fledged plan of reorganization. The independent trustee might call a meeting. He would act in a somewhat informal administrative fashion, as I visualize it. He would bring the various parties together, or see that they got together, and after he had gotten the benefit of their ideas and gotten them together and they traded out "various provisions as to bonds and stocks and unsecured debts, and what not, he would then bring out a plan or plans and submit it to the court."

Mr. Douglas, then Chairman Securities and Exchange Commission, presently a Justice of the Supreme Court of the United States, House Committee Hearing, page 169.

* * * * *

"In other words, by means of the independent trustee, the great power exercised outside the proceedings by the inside few will be exercised within the proceedings for the benefit of investor. The increment of value inherent in power will be appropriated for investors rather than for reorganizers. Some will brand this as unworkable, onerous, and inflexible. All sorts of so-called practical reasons will be marshaled against it. Nevertheless, the independent trustee is the key to real reform. In comparison, the other reforms are secondary. Without

The Supreme Court gave clear and positive expression of the mandate of Section 169 in *Securities and Exchange*

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it the other reforms would be indirect rather than direct approaches to the problem of breaking the strangle hold which the inside few have had over these proceedings."

Mr. Douglas,
House Committee Hearing, page 176-7 (b).

REPORT NO. 1409, HOUSE OF REPRESENTATIVES, SEVENTY-FIFTH CONGRESS, FIRST SESSION, JULY 29, 1937, COMMITTEE ON THE JUDICIARY, CONCERNING H. R. 8046 (THE CHANDLER ACT)

* * * * *

"Under the bill the independent trustee will serve as the focal point for formulation and negotiation of a plan of reorganization. This important function under the present system has been left to the inside few. That normally has meant leaving it to the management and the investment bankers. It should no longer be left in these hands, since those persons too often have interests conflicting with those of the investors."

House Report, page 44.

"* * * * The trustee, as a representative of the court, plays an active role in the formulation and negotiation of plans, and supplies scrutiny and control thereof in the interest of creditors and stockholders. In handling the suggestions of proposals for plans, the independent trustee would act in an informal administrative manner. He is made the active head of the reorganization process; he would provide an intermediate forum and round table where creditors and stockholders could be heard and could negotiate. In short, vital functions which in the past have been performed by inside groups or by protective committees seeking personal profit, will be vested in the trustee—with the advice and consent of creditors and stockholders and subject to court supervision. No longer will the basic, all-important phases of reorganization be performed by groups which have a selfish interest to protect and promote. Heretofore these groups have thrived because they have provided leadership for investors where otherwise there would be anarchy; because they have seized the reins and produced action and provided direction—regardless of their destination. Under the bill these functions will be performed by a distinterested person appointed by the court with the opportunity to interested persons to express their views on the appoihtment."

House Report, pages 44-45.

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REPORT NO. 1916, CALENDAR NO. 2022, APRIL 20 (CALENDAR DAY MAY 27,) 1938, SENATE, SEVENTY-FIFTH CONGRESS, THIRD SESSION, COMMITTEE ON THE JUDICIARY, CONCERNING H. R. 8046 (THE CHANDLER ACT)

"Section 169 places upon the trustee the primary responsibility for the submission of a plan to the court, within a time to be fixed by the judge. It provides for the fixing of a subseqnent hearing thereon, to consider any objections to the plan and any proposals put forward by individual creditors and stockholders, or by the debtor."

Summary of Section 169 Senate Report,
page 30.

Commission v. *U.S.R. & I. Co.*, 310 U.S. 434.

Indeed, the District Court itself recognized in May of 1944 the intent of Congress that trustees should formulate plans; for in the consolidated equity causes involving these companies, the District Court said in its opinion of May 19, 1944:

> "In a bankruptcy reorganization, the Court appoints a disinterested Trustee, whose duty it is to prepare a reorganization" (Pet Appx. 435, p. 436).

It is appellants' position that, since the requirement in question is absolute in tenor, the failure to comply with it is a fatal defect in the proceedings and the appellants need not show any exceptional or extraordinary circumstances requiring compliance with the unmistakable command of Congress.

But, nevertheless, exceptional and extraordinary circumstances are present that indicate a very practical necessity for compliance with this provision in the instant matter. The Continental Illinois National Bank and Trust Company is trustee under both the consolidated mortgage securing the Series A and Series B bonds and under the purchase money mortgage. The Series A bonds and the purchase money bonds both participate in the plan; the Series B bonds do not. Therefore the District Court suffered this bank to occupy the inconsistent position of trustee for three separate groups of bondholders, whose interests were not only competitive but conflicting. This trustee declined to take any action under the plan for the obvious reason that if it asserted objections on behalf of the Series B Bondholders, who took nothing, those objections would militate against the Series A Bondholders and the purchase money bondholders. There was, therefore, every practical reason why the District Court should have

required its trustee to determine whether the plan in question was fair to security holders whose own trustee occupied not a dual but a treble position in the case. But this latter point, although it emphasizes a practical reason why the court's trustees should have acted, is unnecessary because Section 169 of the Act makes it mandatory upon the court to receive a report from its own trustee either proposing a plan or explaining "why a plan cannot be effected" and this requirement was not complied with.

VI.

The orders appealed from were not only erroneous but void because the plan was never submitted to the Illinois Commerce Commission.

Section 178 of Chapter X provides as follows:

> "Sec. 178. In case a debtor is a public utility corporation, wholly intrastate, subject to the jurisdiction of a State commission having regulatory jurisdiction over such debtor, a plan shall not be approved, as provided in section 174 of this Act, *unless such State commission shall have first certified its approval of such plan as to the public interest therein and the fairness thereof.* Upon its failure to certify its approval or disapproval within thirty days, or such further time as the court may prescribe, after the submission of the plan to it, as provided in section 177 of this Act, the public interest shall, for the purposes of such approval and of the confirmation of the plan, not be deemed to be affected by the plan." (Emphasis supplied.)

The diction of this provision is peremtory and its meaning is clear. The District Court itself said in its opinion of May 19, 1944 "A reorganization of these utility corporations cannot be effected without the approvals of the State Commission which are required by law." (Pet. Appx. 435, p. 437). But the instant plan has never been submitted to the Illinois Commerce Commission.

We submit that the plan now under advisement and the orders approving and confirming it are not only erroneous but are wholly void, since bankruptcy proceedings are statutory prerequisites to the exercise of bankruptcy jurisdiction are themselves jurisdictional.

But lest there might otherwise lurk the slightest doubt as to whether Congress meant what it said when it enacted, in the language above quoted, that "a plan shall not be approved * * * unless such State commission shall have first certified its approval of such plan as to the public interest therein and the fairness thereof," we append in the margin brief excerpts from the legislative history of Section 178 that leave no question as to the intent and will of Congress.[20]

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[20] Report No. 1916, Calendar No. 2022, April 20 (Calendar Day May 27,) 1938, Senate, Seventy-Fifth Congress, Third Session, Committee on the Judiciary, Concerning H. R. 8046 (The Chandler Act).

"14. **Approval by State commissions**—(Sec. 178, p. 142).The House bill did not include the provision of section 77B **which requires the approval, by State commissions possessing regulatory jurisdiction over intrastate public-utility corporations, of plans of reorganization for such corporations. This jurisdiction is in effect preserved in section 224 of the House bill, but your committee considers it desirable to remove any ambiguity with respect thereto by restoring to the bill the language of the present law.**"—Senate Report, page 6.

* * * * *

"Section 178, which is also derived from section 77B (e) (2), **contains the further requirement of approval of plans in the case of intrastate public utilities by commissions possessing the power and duty to do so under the appropriate State law.** Of course, the jurisdiction over public utility corporations granted by other statutes, as, for example, the jurisdiction of the Securities and Exchange Commission under the Public Utility Holding Company Act of 1935, is in no way to be affected by any of the provisions of this chapter."—Summary of Section 178, Senate Report, p. 31.

CONCLUSION.

Chapter X requires that all due efforts be given to the development and execution of a plan of reorganization of the Surface Lines System prior to liquidation by sale of the assets of the several estates. In *Continental Illinois National Bank & Trust Co., et al.*, v. *Chicago, Rock Island & Pacific Railway Company, et al.*, 294 U. S. 648, at page 676, the court, speaking in reference to the question of an injunction, restraining the sale of pledged securities, and the validity of reorganizations under the bankruptcy Act, held in part:

> "• • • But a proceeding under Section 77 is not an ordinary proceeding in Bankruptcy. It is a special proceeding which seeks only to bring about a reorganization, if a satisfactory plan to that end can be devised. And to prevent the attainment of that object is to defeat the very end and the accomplishment of which was the sole aim of the Section, and thereby to render its provisions futile. • • • "

This pronouncement applies with equal force to proceedings under Chapter X.

In *Case* v. *Los Angeles Lumber Products Co. Ltd.*, 308 U. S. 106, at p. 144, the Supreme Court of the United States said:

> "At the outset it should be stated that where a plan is not fair and equitable as a matter of law it cannot be approved by the court even though the percentage of the various classes of security holders required by Section 77B (f) for confirmation of the plan has consented. It is clear from a reading of Section 77B (f) that the Congress has required both that the required percentages of each class of security holders approve the plan and that the plan be found to be 'fair and

equitable.' The former is not a substitute for the latter. The court is not merely a ministerial register of the vote of the several classes of security holders. All those interested in the estate are entitled to the court's protection. • • • "

For the reasons developed in this brief, Petitioners submit that this court should grant its writ of *certiorari* and that the orders appealed from should be reversed.

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APPENDIX I.

The Mueller Act, L. 1903, p. 285:

"Section 1. That every city of this State shall have the power to own, construct, acquire, purchase, maintain and operate street railways within its corporate limits, and to lease the same or any part of the same to any company incorporated under the laws of this State for the purpose of operating street railways for any period not longer than twenty years on such terms and conditions as the city council shall deem for the best interests of the public.

"But no city shall proceed to operate street railways unless the proposition to operate shall first have been submitted to the electors of such city as a separate proposition and approved by three-fifths of those voting thereon. It shall be lawful for any such city to incorporate in any grant of the right to construct or operate street railways a reservation of the right on the part of such city to take over all or part of such street railways, at or before the expiration of such grant, upon such terms and conditions as may be provided in the grant; it shall also be lawful to provide in any such grant that in case such reserved right be not exercised by the city and it shall grant a right to another company to operate a street railway in the streets and parts of streets occupied by its grantee under the former grant the new grantee shall purchase and take over the street railway of the former grantee upon the terms that the city might have taken it over and it shall be lawful for the city council of any city to make a grant containing such a reservation, for either the construction or operation or both the construction and operation of a street railway in, upon and along any of the streets or public ways therein, or portions thereof, in which street railway tracks are already located at the

time of the making of such grant, without the petition or consent of any of the owners of the land abutting or fronting upon any street of public way, or portion thereof, covered by such grant."

• • •

"For the purpose of acquiring street railways either by purchase or construction as provided for in this Act, or for the equipment of any such street railways, any city may borrow money and issue its negotiable bonds therefor, pledging the faith and credit of the city; but no such bonds shall be issued unless the proposition to issue the same shall first have been submitted to the electors of such city and approved by two-thirds of those voting thereon, nor in an amount in excess of the cost to the city of the property for which said bonds are issued ascertained as elsewhere provided in this Act and ten (10) per cent of such cost in addition thereto. In the exercise of the powers, or any of them, granted by this act, any such city shall have the power to acquire, take and hold any and all necessary property, real, personal or mixed for the purposes specified in this Act, either by purchase or condemnation in the manner provided by law for the taking and condemning of private property for public use but in no valuation of street railway property for the purpose of any such acquisition except of street railways now operated under existing franchises shall any sum be included as the value of any earning power of such property or of the unexpired portion of any franchise granted by said city. In case of the leasing by any city of any street railway owned by it, the rental reserved shall be based on both the actual value of the tangible property and of the franchise contained in such lease, and such rental shall not be less than a sufficient sum to meet the annual interest upon all outstanding bonds or street railway certificates issued by said city on account of such street railway."